2003 WI 46

SUPREME COURT OF WISCONSIN

Trinity Evangelical Lutheran Church and School-Freistadt,
Plaintiff-Respondent-Cross Petitioner,
v.
Tower Insurance Company,
Defendant-Appellant-Petitioner

No. 01-1201 (L.C. No. 98-CV-0108)
STATE OF WISCONSIN IN SUPREME COURT

FILED MAY 23, 2003
Cornelia G. Clark
Clerk of Supreme Court

NOTICE
This opinion is subject to further editing and modification. The final version will appear in the bound volume of the official reports.

REVIEW of a decision of the Court of Appeals. Reversed in part and affirmed in part.

1. N. PATRICK CROOKS, J. This case involves an insurance action where, as a result of mistake, the insurance policy failed to provide hired and non-owned automobile coverage that the insured requested. After Tower Insurance Company (Tower) learned of the mistake, it failed in its duty to its insured, Trinity Evangelical Lutheran Church and SchoolFreistadt (Trinity) to investigate properly and evaluate reasonably. It initially refused to backdate coverage when the error was discovered after an accident occurred. The pivotal dispute in this case centers on what Tower should have done once it became aware of the mistake.

2. The circuit court, the Honorable Marianne E. Becker presiding, determined that Trinity was entitled to reformation of the insurance policy as a matter of law. The circuit court further concluded that Tower's conduct constituted bad faith under the standard set forth in *Anderson v. Continental Insurance Co.*, 85 Wis. 2d 675, 691, 271 N.W.2d 368 (1978), and accordingly granted summary judgment to Trinity pursuant to Wis. Stat. § 802.08(6) (1999-2000).[1] A jury trial was then held on the issue of damages, and $3,500,000 in punitive damages were awarded to Trinity. Tower's motions after verdict were denied, and judgment was entered on the verdict on March 15, 2001.

3. The court of appeals upheld the punitive damages award of $3,500,000 by applying a de novo standard of review and a "gross excessiveness test." The decision by the court of appeals was made contingent on a trial with a finding of bad faith. The court of appeals found that there were genuine issues of material fact on the claim of bad faith, and therefore it reversed the circuit court's grant of summary judgment on that claim.

4. Two issues must be resolved. First, whether the court of appeals was correct in reversing summary judgment on the bad faith claim, and second, what standard of review should be applied when an appellate court reviews a jury's punitive damages award. We must also determine, applying the relevant factors, whether the jury award of $3,500,000 in punitive damages should be upheld.

5. We conclude that the circuit court properly granted summary judgment on the issue of bad faith. We also

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[1] All subsequent references to the Wisconsin Statutes are to the 1999-2000 version unless otherwise indicated.

hold that the appropriate standard of review to be applied in reviewing a punitive damage award is de novo review, and that when the relevant factors are considered, the punitive damages award should be allowed to stand. Therefore, we reverse, in part, the court of appeals' decision on the grant of summary judgment, but we affirm its decision upholding the award of punitive damages.

I. FACTS

6. Trinity Evangelical Church and School (Trinity) offers religious services as well as a grade school to approximately 234 grade school age children in Mequon, Wisconsin. In 1994, Trinity was interested in renewing its hired and non-owned automobile insurance coverage that it carried, because its teachers had occasion to transport students to and from certain functions in the course of their employment using their own vehicles.

7. Trinity sought renewal quotations from various carriers including Tower Insurance Company (Tower) who was represented by their agent Jim Rodrian (Rodrian). Trinity explained to Rodrian its need for hired and non-owned coverage. Rodrian then passed this information on to Harold Fischer (Fischer), an underwriter at Tower. Fischer gave Rodrian a quote, which Rodrian believed included the requested coverage, and Rodrian subsequently provided the quote to Trinity, who accepted it, believing it would be covered for hired and nonowned automobiles.

8. On February 10, 1994, Rodrian sent Trinity's preapplication binder, which included information on this requested form of coverage. However, Rodrian inadvertently failed to check the hired and non-owned box on Trinity's insurance application. Tower issued the policy without any of

the parties involved being aware of the omission of the requested coverage.

9. On January 24, 1995, Lorrie Erdman, a teacher at Trinity, while transporting students from the school in the course of her employment, using her own vehicle, ran a stop sign and collided with another vehicle. The collision resulted in serious injuries to the other vehicle's driver and passenger.

10. Trinity notified Rodrian of the potential claim. Upon review of the policy, Rodrian discovered his omission. Rodrian drafted a letter to Carol Blackwell (Blackwell), a district manager in Tower's underwriting department, dated January 31, 1995, informing Tower of the accident and of the fact that he mistakenly failed to request hired and non-owned automobile coverage on the application. Rodrian also requested that Tower backdate Trinity's coverage.

11. In response to Rodrian's letter, Blackwell drafted a memo to Gene Gallagher, the vice president and director of operations at Tower. Blackwell's memo summarized the circumstances surrounding Rodrian's error, and asked for direction as to how to handle Rodrian's request to backdate coverage.

12. Within twenty-four to forty-eight hours, Gallagher instructed Blackwell to inform Rodrian that Tower would not backdate Trinity's coverage.[2]

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[2] It is Trinity's position that Gallagher did nothing to investigate Tower's duty to Trinity before making his decision, and that this non-investigation, among other things, constituted bad faith on Tower's part. Trinity points out that Gallagher made his decision without ever contacting Tower's in-house attorney for advice on the matter, and without ever contact-

(continued...)

13. Gallagher sent a handwritten note to Blackwell, which describes his decision:

> Carol–Your referral says that this is agency error and not ours. We didn't get request to provide [hired and non-owned coverage] didn't get copy of binder till now, so [we] don't have any reason to backdate. Suggest agent [Jim Rodrian] alert his E and O carrier if he hasn't already. I'm not going to put backdate and add with uncertainty as to possible exposure. We could be facing big dollars due to liab[ility]?? If you want to discuss further let me know. Gene

On February 2, 1995, Blackwell met with Rodrian to inform him of Tower's decision not to backdate coverage.

14. Thereafter, Tower was asked on several occasions to reconsider its position. One request for reconsideration came from Jim Reynolds, the adjuster for Rodrian's Errors and Omissions (E & O) carrier. This letter, mailed to Gallagher, included a citation to *Trible v. Tower Insurance Co.*, 43 Wis.2d 172, 168 N.W.2d (1969).[3] Gallagher did not read the case, and

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2 (...continued)
ing Trinity to verify Rodrian's representation.

3 *Trible* is the seminal case in Wisconsin addressing the obligation of an insurer to reform an insurance contract upon the discovery of a mutual mistake in the issuance of the written policy. The facts of *Trible* are nearly identical to the facts presented to Tower at the time it denied coverage to Trinity. *Trible* involved an insurance agent tied to an insurer via an agency contract. There was an error in requesting
(continued...)

Tower did not change its decision.

II. PROCEDURAL BACKGROUND

15. A suit arising out of the accident was filed in 1998. On May 18, 1998, Tower filed a motion for summary judgment asking to be dismissed as a party in the case. This motion was based solely on language of the written policy, and the motion failed to bring to the court's attention that Tower had been informed by its agent that the written policy was in error. Specifically, Tower failed to inform the court in its motion that its agent had requested the policy to be backdated and that Tower had denied the agent's request.

16. In response to Tower's motion for summary judgment, Trinity hired an attorney to represent it on the question of insurance coverage, and filed a cross-claim for reformation and breach of contract. Shortly thereafter, Tower withdrew its motion for summary judgment.

17. On September 28, 1998, Trinity deposed Fischer, the Tower underwriter who dealt with the insurance agent, Rodrian, in regard to Trinity's policy. During Fischer's deposition, Trinity discovered that in June 1995, four months after Blackwell had met with Rodrian to inform him of Tower's decision, an investigator hired by Rodrian had tracked down Fischer and obtained a signed statement from him. The

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[3] (...continued)
coverage, thereby creating a "mutual mistake" (*see* note 4), and the insurer later discovered that the insured had, in fact, requested the coverage. This court in *Trible* concluded that reformation of the erroneous insurance policy was appropriate. It is also important to note that Tower was the defendant in *Trible v. Tower Insurance Co.*, 43 Wis. 2d 172, 168 N.W.2d 148 (1969).

statement made it clear that Rodrian had indeed asked Fischer to include hired and non-owned automobile coverage in Trinity's policy.

18. Two days later, Tower stipulated to reform Trinity's policy to include non-owned and hired coverage at the time of the accident. Tower also paid approximately $490,000 to discharge Trinity's liability in its entirety in the underlying accident suit. Trinity subsequently amended its cross-claim to assert a bad faith cause of action against Tower.

19. In response, Tower filed a motion for summary judgment seeking dismissal of the bad faith claim. In a written decision, the Circuit Court of Waukesha County, Honorable Marianne E. Becker presiding, held that Trinity was entitled to reformation of the insurance policy as a matter of law. The circuit court additionally found that Tower's conduct constituted bad faith under the standard set forth in *Anderson v. Continental Insurance Co.*, 85 Wis. 2d 675, 691, 271 N.W.2d 368 (1978), and accordingly granted summary judgment for Trinity pursuant to Wis. Stat. § 802.08(6).

20. Following the circuit court's decision, the only factual issue left for determination by a jury was whether punitive damages should be awarded. After several days of testimony, including testimony from Gallagher that he had no knowledge of principal/agency law, the law of reformation, Wisconsin's Unfair Claims Practices Act, or the *Trible* case, the jury determined that Tower had acted "in an intentional disregard of the rights of the plaintiff" awarding $3,500,000 in punitive damages to Trinity.

21. Tower's motions after verdict were denied and judgment was entered on the verdict on March 15, 2001. Tower appealed.

22. The court of appeals upheld the punitive damages award of $3,500,000 by applying a de novo standard of review and a "gross excessiveness test." This decision by the court was made contingent on a trial with a finding of bad faith. The court of appeals held that the circuit court erred in granting summary judgment on the bad faith claim.

23. Tower petitioned for review on the punitive damages award, and Trinity cross-petitioned on the bad faith claim. Review was granted on September 3, 2002.

24. As previously noted, this court must determine whether the court of appeals was correct in reversing the grant of summary judgment on the bad faith claim, and what standard of review should be applied when an appellate court reviews a punitive damages award.

25. When reviewing a grant of summary judgment, the appellate court applies the same standards set forth in Wis. Stat. § 802.08 as the circuit court applies. *Voss v. City of Middleton*, 162 Wis. 2d 737, 748, 470 N.W.2d 625 (1991).

26. It is argued by Tower and by Trinity that when reviewing a circuit court's decision regarding a punitive damages award, the appellate court should apply a de novo standard. *Cooper Indus., Inc. v. Leatherman Tool Group, Inc.*, 532 U.S. 424, 435-36 (2001); *BMW of N. Am., Inc. v. Gore*, 517 U.S. 559 (1996).

27. Tower argues that the appellate court erred in upholding a punitive damages award that was premised on a bad faith finding that was later reversed. In support of its position, Tower maintains that the bifurcation of the bad faith issue and the punitive damages issue prejudices Tower and runs counter to established practice in Wisconsin. In addition, Tower argues that the appellate court erred in upholding a grossly excessive punitive damages award.

28. Trinity, on the other hand, asks this court to affirm the circuit court's decision granting summary judgment on the bad faith issue. Trinity argues that the circuit court properly analyzed and applied Wisconsin's bad faith law. However, Trinity asks that this court affirm the court of appeals' decision upholding the punitive damages award. Trinity argues that upon a de novo review of the facts of this case, it is clear that the punitive damages award is not in violation of due process, nor is it excessive.

III. BAD FAITH CLAIM

29. First, we turn to the question of whether the circuit court properly granted summary judgment on the claim of bad faith. We hold that, based on the facts of this case, only one reasonable inference can be drawn—Tower acted with bad faith toward its insured, Trinity. Consequently, we reverse the court of appeals' decision that reversed the grant of summary judgment on that claim.

30. As noted above, when reviewing a grant of summary judgment, we apply the standards set forth in Wis. Stat. § 802.08. *Robinson v. City of West Allis*, 2000 WI 126, ¶26, 239 Wis. 2d 595, 619 N.W.2d 692; *Voss*, 162 Wis. 2d at 748.

31. Under Wis. Stat. § 802.08(2), summary judgment must be entered "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law."

32. Therefore, the first step in the summary judgment review analysis is to determine whether the pleadings set forth a claim of relief. *Grams v. Boss*, 97 Wis. 2d 332, 338, 294

N.W.2d 473 (1980). Next, if the pleadings meet this initial test, and our review of the record shows that the moving party has made a prima facie case for summary judgment, we examine the record to determine whether there "exist[s] disputed material facts, or undisputed material facts from which reasonable alternative inferences may be drawn, sufficient to entitle the opposing party to a trial." *Id.*

33. *Anderson* sets forth the elements of bad faith. *Anderson*, 85 Wis. 2d at 691. First, an insured must show absence of a reasonable basis for denying policy benefits. *Mowry v. Badger State Mut. Cas. Co.*, 129 Wis. 2d 496, 516, 385 N.W.2d 171 (1986). Absence of a reasonable basis for denying a claim exists when the claim is not "fairly debatable." *Id.* The "fairly debatable" test requires a claim to be investigated properly and the results of that investigation to be subject: to reasonable evaluation and review. *Anderson*, 85 Wis. 2d at 692.

34. According to *Anderson*, an insured must show "the absence of a reasonable basis for denying benefits of the policy " and the insurer's "knowledge or reckless disregard of the lack of a reasonable basis for denying the claim." *Id.* at 691. "[B]ad faith is the absence of honest, intelligent action or consideration based upon a knowledge of the facts and circumstances upon which a decision in respect to liability is predicated." *Id.* at 692. There is a duty of ordinary care and reasonable diligence on the part of an insurer in handling claims, and it must exercise an honest and informed judgment. *Id.* We agree with the court of appeals: "In short, it is proper when applying the bad faith test to determine whether a claim was properly investigated and whether the results of the investigation were subjected to a reasonable evaluation and review." *See Trinity Evangelical Lutheran Church v. Tower Ins. Co.*, 2002 WI App 46, 127, 251 Wis. 2d 212, 641 N.W.2d 504.

35. Applying the above rules to the facts of this case, the pleadings of Trinity set forth a claim for relief.

36. The court of appeals reviewed the record and determined that genuine issues of material fact were in dispute, making summary judgment on the bad faith claim inappropriate. *Trinity*, 251 Wis. 2d at 233. Specifically, the court said: "the facts related to what Tower actually knew and thus whether there was an *intertional* disregard are in dispute." *Id.* (emphasis added).

37. We disagree with the decision of the court of appeals. First, contrary to the test set forth by the court of appeals, Trinity was not required to make a showing of intentional disregard in order to succeed on a claim of bad faith. The appropriate test, as noted above, is whether the insurer acted with "knowledge or reckless disregard of the lack of a reasonable basis for denying the claim." *Anderson*, 85 Wis. 2d at 691. While we note that *Anderson* does say that: "Bad faith by definition cannot be unintentional." The court of appeals, however, appears to have conflated the "intentional disregard" standard required for punitive damages, with the "knowledge or reckless disregard" standard required for bad faith. *See id.*

38. Second, upon an independent review of the record, we conclude that the record in this case clearly indicates that the facts regarding what Tower knew were not in dispute at the time of the granting of summary judgment. While there may be some factual disputes, those disputes do not involve genuine issues of material fact. Indeed, the undisputed material facts in this case lead to only one reasonable inference—an inference of bad faith on the part of Tower. The *Anderson* court stated that "th knowledge of the lack of a reasonable basis may be inferred and imputed to an insurance company where there is a reckless disregard of a lack of a reasonable basis for denial or a reckless

indifference to facts or to proofs submitted by the insured." *Anderson*, 85 Wis. 2d at 693.

39. This case centers on what Tower should have done when it learned its agent made a mistake that adversely affected its insured, Trinity. Tower was put on notice by this court over 30 years ago, when it was the defendant in a nearly identical fact situation. *Trible*, 43 Wis. 2d 172. In this present case, Tower was reminded of that prior decision, but denied coverage nonetheless.

40. The following undisputed material facts illustrate Tower's reckless disregard toward its insured, Trinity. First, the record indicates that Tower, through its prior involvement as the defendant in the *Trible* case, should have understood its obligation to provide the requested coverage to an insured such as Trinity, where a mutual mistake has occurred.[4] Second, the record indicates without dispute that Trinity lacked coverage

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[4] It can be argued here that the mistake was unilateral rather than mutual given there was no error or mistake on the part of Trinity. *Black's Law Dictionary* defines a unilateral mistake as one-sided; relating to only one of two or more persons or things. *Black's Law Dictionary*, 1532 (7th ed. 1999). However, the court in *Trible* and the circuit court and court of appeals in *Trinity* consistently refer to the "mistake" described here and in *Trible* as being a mutual mistake. For example, the court in *Trible* said: "When a policy of insurance is involved, mutual mistake is proven when the party applying for insurance proves that he made certain statements to the agent concerning the coverage desired, but the policy as issued does not provide the coverage desired."

Trible v. Tower Ins. Co., 43 Wis. 2d 172, 182, 168 N.W.2d 148 (1969); *See also, Trinity Evangelical Lutheran Church v. Tower Ins. Co.*, 2002 WI App 46, ¶26, 251 Wis. 2d 212, 641 N.W.2d 504.

due to a mutual mistake attributable to Tower's agent, Rodrian. The court of appeals recognized this undisputed fact. *See Trinity*, 251 Wis. 2d 212, 19.

41. Next, it is undisputed, and recognized by the court of appeals, that Tower, via Gallagher, knew of this mutual mistake when it denied coverage to Trinity. *See id.* (citing to letter to Blackwell). Finally, there is no dispute that Trinity requested that its coverage be backdated, and the court of appeals recognized this undisputed fact. *See id.*

42. It is clear that Tower, knowing of the mutual mistake, failed to take "honest, intelligent action or consideration based upon knowledge of the facts and circumstances" presented to it when it denied coverage to Trinity. *See Anderson*, 85 Wis. 2d at 692. Tower also failed to take such action or consideration when it failed to inform the court of Rodrian's error and his request for backdating. As a result, Tower failed to act in conformity with its duties.

43. In light of the undisputed material facts set forth herein, we conclude that the only reasonable inference that can be drawn is that Tower acted in bad faith. As a result, we agree with the circuit court that summary judgment was appropriate here, and reverse the court of appeals' decision in that regard.

IV. PUNITIVE DAMAGES AND THE STANDARD OF REVIEW

44. We now turn to the issue of the punitive damages award. Tower argues that the appellate court erred in upholding a grossly excessive punitive damages award of $3,500,000 in violation of due process constraints. We disagree, and affirm the decision of the court of appeals upholding that award by the jury.

45. Proof of a bad faith claim does not necessarily make the award of punitive damages appropriate. *Anderson*, 85 Wis. 2d at 697. The intent necessary to maintain an action for bad faith is distinct from what must be shown to recover punitive damages. *Id.*; *see also* Wis. Stat. § 895.85 (3). The factors necessary for an award of punitive damages, require a showing of: (1) evil intent deserving of punishment or of something in the nature of special ill-will; or (2) wanton disregard of duty; or (3) gross or outrageous conduct. *Anderson*, 85 Wis. 2d at 697.[5]

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[5] While the *Anderson* test is phrased somewhat differently than the standard jury instruction that was given on punitive damages, the jury instruction adequately covered the factors that the jury should have considered here. That instruction was as follows:

> Punitive damages may be awarded, if you find that the defendant acted in an intentional disregard of the rights of the plaintiff.
>
> A person acts in an intentional disregard of the rights of the plaintiff if the person acts with a purpose to disregard the plaintiff's rights, or is aware that his or her acts are practically certain to result in the plaintiff's rights being disregarded.
>
> The purpose of punitive damages is to punish a wrongdoer or deter the wrongdoer and others from engaging in similar conduct in the future. Punitive damages are not awarded to compensate the plaintiff for any loss he or she has sustained. A plaintiff is not entitled to punitive damages as a matter of right. Even if you find that the defendant acted in an intentional disregard of the plaintiff's rights, you do not have to award punitive damages. Such damages may be awarded or withheld at your discretion.

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46. Punitive damages may properly be imposed to further a state's legitimate interests in punishing unlawful conduct and deterring its repetition. *BMW*, 517 U.S. at 568. According to Wisconsin law, the award of punitive damages in a particular case is within the discretion of the jury, and "[w]e are reluctant to set aside an award merely because it is large or we would have awarded less." *Jacque v. Steenberg Homes, Inc.*, 209 Wis. 2d 605, 626, 563 N.W.2d 154 (1997).

47. In *Cooper Industries, Inc. v. Leatherman Tool Group, Inc.*, 532 U.S. 424 (2001), the United States Supreme Court held that the Ninth Circuit Court of Appeals erred in applying the less demanding abuse-of-discretion standard when reviewing district court determinations of the constitutionality of an award of punitive damages. Instead, the United States Supreme Court determined that the constitutional issue of punitive damages merits de novo review. *Cooper*, 532 U.S. at 431. In reaching that conclusion, the Court said that the precise

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[5] (...continued)

If you determine that punitive damages should be awarded, you may then award such sum as will accomplish the purpose of punishing or deterring wrongful conduct.

Factors you should consider in answering this question include:

1. The grievousness of the defendant's acts,
2. The potential damage which might have been done by such acts as well as the actual damage, and
3. The defendant's ability to pay. You may consider the defendant's wealth in determining what sum of punitive damages will be enough to punish the defendant and deter the defendant and others from the same conduct in the future.

meaning of concepts like "gross excessiveness" is a fluid concept "that take their substantive content from the particular context [] in which the standard [] is being assessed." *Id.* at 436. The Court went on to say:

> "Independent review is therefore necessary if appellate courts are to maintain control of, and clarify, the legal principles." Again, this is also true of the general criteria set forth in *Gore*; they will acquire more meaningful content through case-by-case application at the appellate level. "Finally, defendant and deter the defendant and others from the same conduct in the future. novo review tends to unify precedent" and "'stabilize the law.'" . . . Justice Breyer made a similar point in his concurring opinion in *Gore*:
>
> "Requiring the application of law, rather than a decisionmaker's caprice, does more than simply provide citizens notice of what actions may subject them to punishment; it also helps to assure the uniform treatment of similarly situated persons that is the essence of law itself."

Id.

48. Similarly, in Wisconsin, in *Management Computer Services*, this court held, in determining whether a jury's award was excessive, that the reviewing court properly reviewed the entire record "*lab inito*" or "de novo," placing no weight on the circuit court's conclusions. *See Management Computer Servs. v. Hawkins, Ash, Baptie & Co.*, 206 Wis. 2d 158, 192 n.32, 557 N.W.2d 67 (1996). We reached that conclusion because the circuit court set forth conclusory reasons for reducing a jury's punitive damages award of $1,750,000 to $650,000, and failed to analyze the evidence or set forth its own reasons for ordering remittitur with particularity. While *Management Computer*

Services is a case involving remittitur, and therefore factually distinguishable, we nevertheless apply the reasons set forth in *Cooper* and extend the de novo review rule in *Management Computer Services* to apply to all situations, remittitur or otherwise, where there is a review of a punitive damages award. Therefore, building upon and extending the rule in *Management Computer Services*, we hold that a de novo standard of review is appropriate when reviewing a circuit court's determination of the constitutionality of punitive damages awards.

49. Although de novo review is the appropriate standard of review, we nevertheless acknowledge that the Due Process Clause of the Fourteenth Amendment imposes substantive limits on the size of a punitive damages award. *Management Computer Servs.*, 206 Wis. 2d at 193. *See also Cooper*, 532 U.S. at 433.

50. An award is excessive, and therefore violates due process, if it is more than necessary to serve the purposes of punitive damages, or inflicts a penalty or burden on the defendant that is disproportionate to the wrongdoing. *Management Computer Servs.*, 206 Wis. 2d at 193 (citing *Tucker v. Marcus*, 142 Wis. 2d 425, 446, 418 N.W.2d 818 (1988); *Wangen v. Ford Motor Co.*, 97 Wis. 2d 260, 303, 294 N.W.2d 437 (1980); *Fahrenberg v. Tengle*, 96 Wis. 2d 211, 234, 291 N.W.2d 516 (1980)). As noted by this court in previous decisions, the purpose of punitive damages is to punish the wrongdoer, and to deter the wrongdoer and others from similar conduct, rather than to compensate the plaintiff for any loss. *Id.* (citing *Wangen*, 97 Wis. 2d at 303; *Malco v. Midwest Aluminum Sales, Inc.*, 14 Wis. 2d 57, 64, 109 N.W.2d 516 (1961)). *See also Cooper* at 432 (citing *Gertz v. Robert Welch, Inc.*, 418 U.S. 323, 350 (1974)).

51. In *Jacque*, we reiterated the decision of the United States Supreme Court in TXO, and held that only when an award can be fairly categorized as "grossly excessive," in

relation to the state's interests in punishment and deterrence, does it enter the zone of arbitrariness that violates due process. *Jacque*, 209 Wis. 2d at 627 (citing *TXO Prod. Corp. v. Alliance Res. Corp.*, 509 U.S. 443, 454 (1993)). Furthermore, the test for "grossly excessive[ness]" stems from a basic notion of fairness that a party should receive fair notice, not only of the conduct that will subject it to punishment, but also of the severity of the penalty that a state may impose. *BMW*, 517 U.S. at 574; *Jacque*, 209 Wis. 2d at 627.

52. Accordingly, in determining whether an award of punitive damages is excessive, the United States Supreme Court has applied a three-part test. The test asks the reviewing court to weigh: (1) the degree of egregiousness or reprehensibility of the conduct; (2) the disparity between the harm or the potential harm suffered and the punitive damages award; and (3) the difference between the punitive damages and the possible civil or criminal penalties imposed for the conduct. *BMW*, 517 U.S. at 575; *State Farm Mut. Auto. Ins. Co. v. Campbell*, 538 U.S., 123 S. Ct. 1513 (2003).[6]

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[6] In a recent opinion, the United States Supreme Court reiterated the three-prong test of *Gore* and said:

> [W]e instructed courts reviewing punitive damages to consider three guideposts: (1) the degree of reprehensibility of the defendant's misconduct; (2) the disparity between the actual or potential harm suffered by the plaintiff and the punitive damages award; and (3) the difference between the punitive damages awarded by the jury and the civil penalties authorized or imposed in comparable cases. We reiterated the importance of these three guideposts in *Cooper Industries* and mandated appellate courts to conduct *de novo* review of a trial court's application of them to the jury's award. Exacting appellate review ensures that an award of punitive damages is based upon an 'application of law, rather than a

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53. When applying a virtually identical test, Wisconsin courts have been encouraged to consider, from the following, those factors which are most relevant to the case, in order to determine whether a punitive damages award is excessive:

1. The grievousness of the acts;

2. The degree of malicious intent;

3. Whether the award bears a reasonable relationship to the award of compensatory damages;

4. The potential damage that might have been caused by the acts;

5. The ratio of the award to civil or criminal penalties that could be imposed for comparable misconduct, and

6. The wealth of the wrongdoer.

Management Computer Servs., 206 Wis. 2d at 194 (citing *BMW*, 116 S. Ct. at 1598-60; Tucker, 142 Wis. 2d at 446-47; *Brown v. Maxey*, 124 Wis. 2d 438, 439, 369 N.W.2d 677 (1985); *Wangen*, 97 Wis. 2d at 302; *Dalton v. Meister*, 52 Wis. 2d 173, 180-81, 188 N.W.2d 494 (1971), *cert. denied*, 405 U.S. 934 (1972); *Malco*, 14 Wis. 2d at 66).

54. With the above rules in mind, we now turn to the facts of this case. As an insurance company doing business in

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[6] (...continued)
decisionmaker's caprice.'

State Farm Mut. Auto. Ins. Co. v. Campbell, 538 U.S.___, 123 S. Ct. 1513 (2003).

Wisconsin, Tower has an implied duty of good faith and fair dealing, and our law has developed such that this duty encompasses the obligation to investigate properly and evaluate reasonably disputed coverage claims. *Prosser v. Leuck*, 225 Wis. 2d 126, 138, 592 N.W.2d 178 (1999). Here, the state has a legitimate interest in deterring insurance companies such as Tower from engaging in acts of bad faith. Furthermore, the state has an interest in deterring Tower, and others, from ignoring applicable decisions of this court as to its duty to its insured, and then later claiming ignorance of what such a duty entails. The $3,500,000 punitive damages award against Tower will serve the legitimate state interest in deterrence, as well as in punishment. Consequently, the punitive damages award will send a message not only to Tower, but to other insurance companies as well, that ignoring its duties as an insurer is not acceptable and might very well result in substantial punitive damages.

55. Since we have determined that the punitive damages award accomplishes the legitimate state interests of punishment and deterrence, we now weigh the factors set forth in BMW against these interests. *See Jacque*, 209 Wis. 2d at 627.

56. However, the evidence must be viewed in the light most favorable to the plaintiff, and a jury's punitive damages award will not be disturbed, unless the verdict is so clearly excessive as to indicate passion and prejudice. *Id.* at 626-27.

57. First, we analyze the degree of grievousness or reprehensibility involved. As we declared in *Jacque*, "[t]he most important indicium of the reasonableness of a punitive damage award is the degree of reprehensibility of the defendant's conduct." *Jacque*, 209 Wis. 2d at 628; *see also BMW*, 517 U.S. at 576 n.23 (citing David G. Owen, *A Punitive Damages Overview: Functions, Problems and Reform*, 39 Vill. L. Rev. 363, 387 (1994)) ("The flagrancy of the misconduct is

thought to be the primary consideration in determining the amount of punitive damages.") *Id.* The grievousness or reprehensibility of Tower's conduct is clear from the record. Tower engaged in prohibited conduct while knowing or recklessly disregarding the lack of a reasonable basis for denying the claim. This court told Tower more than 30 years ago about the duty of an insurer to reform an insurance policy upon a discovery of mutual mistake. *See Trible v. Tower Ins. Co.*, 43 Wis. 2d 172, 168 N.W.2d 148 (1969). Not only was Tower told what to do in such a situation of mutual mistake, but Tower was reminded of this decision by Jim Reynolds in his letter.

58. Recently, the United States Supreme Court reiterated the rules for punitive damages with regard to repeat offenders, or "recidivist[s]". *Campbell*, 538 U.S. at ___. The United States Supreme Court said:

> Although "[o]ur holdings that a recidivist may be punished more severely than a first offender recognize that repeated misconduct is more reprehensible than an individual instance of malfeasance," *Gore*, *supra*, at 577, in the context of civil actions courts must ensure the conduct in question replicates the prior transgressions. *TXO*, 509 U.S. at 462 n. 28 (noting that courts should look to "'the existence and frequency of similar past conduct'") (quoting *Haslip*, 499 U.S. at 21-22).

Id.

59. Tower disregarded the law and its duty to an insured like Trinity not once-but twice. Such repeated disregard for the law and its duty indeed seems egregious and reprehensible. *See BMW*, 517 U.S. at 576-77; *Jacque*, 209 Wis. 2d at 628. In viewing the evidence according to the rules set forth in *Jacque* and *Campbell*, the bad faith in this case involved Tower's

intentional disregard of its duty to investigate diligently to ascertain and evaluate the facts and circumstances underlying the issuance of the policy and the accident, in order to arrive at a good faith decision. *See Prosser*, 225 Wis. 2d at 138.

60. As stated previously, Gallagher, as the representative of Tower, made a series of decisions that illustrate bad faith on behalf of Tower. These acts of bad faith also buttress a determination of the egregiousness of Tower's conduct. The record indicates that Tower, through its prior involvement as the defendant in the *Trible* case, should have understood its obligation to provide coverage to Trinity where clearly a mutual mistake had occurred. As noted in *Campbell*, recidivists, or repeat offenders, may be punished more severely, in that their conduct is viewed to be more "reprehensible than an individual instance of malfeasance." *Campbell*, 538 U.S. at ____.

61. Trinity lacked coverage due to a mutual mistake attributable to Tower's agent, Rodrian. The court of appeals recognized this. *See Trinity*, 251 Wis. 2d 212. Furthermore, it is undisputed, and recognized by the court of appeals and the circuit court, that Tower, through Gallagher, knew of this mutual mistake when it denied coverage to Trinity. *See id.* ¶9

62. In addition to the undisputed material facts, it is important to note that the record indicates that Gallagher, on behalf of Tower, made the decision to deny coverage without investigating Rodrian's requests for backdating, and without seeking available in-house legal counsel. Not only did Gallagher, on behalf of Tower, fail to investigate the situation properly, but the record reveals that Gallagher failed to contact Fischer, Tower's own underwriter, with whom Rodrian worked on the Trinity policy, about whether he understood Trinity to have requested hired and non-owned coverage. Furthermore, Tower decided to ask for summary judgment without informing the court of the dispute regarding Rodrian's error, and the

request for backdating. These decisions, acts, and omissions on the part of Gallagher, on behalf of Tower, illustrate a continuing, egregious, and flagrant pattern of disregard toward Tower's duty owned to its insured, Trinity. As a result, we conclude that the egregiousness and reprehensibility factor has been met under the *BMW* test.

63. Next, we measure the disparity between the harm or potential harm suffered by Trinity and the punitive damages award. *Jacque*, 209 Wis. 2d at 628-29. When compensatory damages are awarded, the reviewing court is to consider whether the award bears a reasonable relationship to the award of compensatory damages, and to possible civil or criminal penalties. *Id.* at 629. Compensatory damages represent the actual harm inflicted on the plaintiff. *Id.* Wisconsin law expressly rejects the use of a fixed multiplier, either a fixed ratio of compensatory to punitive damages or of civil or criminal penalties to punitive damages, to calculate the amount of reasonable punitive damages. *Management Computer Servs.*, 206 Wis. 2d at 194. *Accord Cooper*, 532 U.S. at 434, and *BMW*, 517 U.S. at 582. However, we have held that in the appropriate case, a comparison of the compensatory damages and the punitive damages award is important. *Jacque*, 209 Wis. 2d at 629.[7]

64. With regard to the second guidepost, the disparity of harm or potential harm and the punitive damages award, the United States Supreme Court recently held:

> Nonetheless, because there are no rigid benchmarks that a punitive damages award may not surpass,

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[7] At trial, the attorney for Trinity claimed that Tower's alleged bad faith actions exposed Trinity to $490,000 in potential harm.

> ratios greater than those we have previously upheld may comport with due process where "a particularly egregious act has resulted in only a small amount of economic damages." *Ibid.*, *see also ibid.* (positing that a higher ratio *might* be necessary where "the injury is hard to detect or the monetary value of noneconomic harm might have been difficult to determine"). The converse is also true, however. When compensatory damages are substantial, then a lesser ratio, perhaps only equal to compensatory damages, can reach the outermost limit of the due process guarantee. The precise award in any case, of course, must be based upon the facts and circumstances of the defendant's conduct and the harm to the plaintiff.

Campbell, 538 U.S. at ___. .

65. The facts and circumstances of Tower's conduct and Trinity's harm are clear. At trial, both parties were given the opportunity to introduce evidence and argue on this issue. Tower introduced evidence that the only potential damage in this case was $17,000; Trinity introduced evidence of a harm of $490,000 had Tower succeeded on its motion for summary judgment. The punitive damages award represents a 7:1 ratio of punitive damages to compensatory damages, if Trinity's position is applied.

66. Finally, under the *BMW* test, we engage in a comparison of the punitive damages award and the civil or criminal penalties that could be imposed for comparable misconduct. *Jacque*, 209 Wis. 2d at 630. As noted by the United States Supreme Court:

> The third guidepost in *Gore* is the disparity between the punitive damages award and the "civil penalties

> authorized or imposed in comparable cases." We note that, in the past, we have also looked to criminal penalties that could be imposed. The existence of a criminal penalty does have bearing on the seriousness with which a State views the wrongful action. When used to determine the dollar amount of the award, however, the criminal penalty has less utility.

Campbell, 538 U.S. at ___.

67. The court of appeals found this factor "largely irrelevant" to the case at hand. *See id.* In reaching that conclusion, the court of appeals said that:

> [t]he legislature has not put into place a criminal or civil statute prohibiting insurance carriers from intentionally disregarding the contractual rights of an insured and rejecting claims on the basis of their own economic self-interest. Thus, as our supreme court held in *Jacque*, when a legislature has not prescribed penalties for the type of conduct engaged in by the defendant, this third guidepost becomes immaterial.

Trinity Evangelical Lutheran Church v. Tower Ins. Co., 2002 WI App 46, 141, 251 Wis. 2d 212, 641 N.W.2d 504.

68. However, the legislature has provided a criminal penalty, including a fine of up to $10,000, for any violation of "any insurance statute or rule of this state." Wis. Stat. § 601.64(4). The Wisconsin Administrative Code contains insurance rules that prohibit unfair settlement practices, including the "[f]ailure to attempt in good faith to effectuate fair and equitable settlement of claims submitted in which liability has become reasonably clear." Wis. Admin. Code § Ins. 6.11 (3) (a)

(4) (Jan., 2002). In this case, as noted previously, a 7:1 ratio results if Trinity's position on compensatory damages is accepted. Furthermore, as noted above, a criminal penalty has "less utility" when used to determine the dollar amount of the punitive damages award. *Campbell*, 538 U.S. at ___.

69. The factors discussed are the ones most relevant in this case. As noted previously, there are other factors that may be relevant given the nature of the case at hand. *See Management Computer Servs.*, 206 Wis. 2d at 194. Defendant's wealth is oftentimes a significant factor. In this case, the evidence presented to the jury through the testimony of Trinity's expert, Robert Niendorf, appears sufficient to justify the size of the punitive damages award.[8]

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[8] Over Tower's objections and motion to bar Niendorf's testimony, the circuit court admitted Ninedorf's conclusion that Tower is able to pay a punitive damages award in one of three ways: by liquidating its assets (at the end of 1999, the Company had a net worth of $24,600,000); by drawing on insurance reserves, or "retained earnings," for a sum of approximately $15,000,000; or by restructuring its debt-equity ratio, evidence claiming that Niendorf's analysis improperly aggregated the financial position of Tower and its parent company, Atlas redacted portion of Niendorf's testimony, but allowed Niendorf to testify to his conclusions.

The court of appeals at paragraphs 31-32 in its opinion said:

> [F]or our purposes. . . contrary to Tower's assertion, Niendorf's testimony did not include improper information about Tower's parent company . . . . It does not appear that Niendorf's theories regarding Tower's ability to pay relied on the financial well-being of Atlas. And finally, each source of money listed as available to satisfy a punitive damages judgment was totally internal to the financial assets

(continued...)

V. CONCLUSION

70. In summary, we conclude that the circuit court properly granted summary judgment on the issue of Tower's bad faith. No other reasonable inference can be drawn from the facts presented. Therefore, we reverse the court of appeals' decision in part. We also hold that the appropriate standard to be applied in reviewing a punitive damages award is a de novo review standard. Applying that standard, and the factors most relevant in this case, we affirm the court of appeals decision upholding the award of punitive damages by the jury.

By the Court. The decision of the court of appeals is reversed in part and affirmed in part.

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[8] (...continued)
of Tower. We hold that the process was untainted by Niendorf's testimony.

Trinity, 251 Wis. 2d 212, ¶¶31-32.

71. DAVID T. PROSSER, J. (dissenting). Justice Sykes has written a compelling dissent. It ably expresses several of my concerns, and I join it without reservation. I write separately because, for me, this case raises disconcerting questions about the future of trial by jury in civil cases.

72. The Wisconsin Constitution provides that: "The right of trial by jury shall remain inviolate, and shall extend to all cases at law without regard to the amount in controversy; but a jury trial may be waived by the parties in all cases in the manner prescribed by law." Wis. Const. art. I, § 5.

73. We have said repeatedly that the right to trial by jury preserved by the constitution is the right as it existed at the time of the adoption of the constitution in 1848. *Town of Burke v. City of Madison*, 17 Wis. 2d 623, 635, 117 N.W.2d 580 (1962); *see also State v. Hansford*, 219 Wis. 2d 226, 234-37, 580 N.W.2d 171 (1998).

74. Summary judgment did not exist as part of Wisconsin law in 1848. There should thus be sensitivity to the impact of summary judgment on jury trials as summary judgment practice evolves.

75. In the early part of the twentieth century there were numerous cases testing the compatibility of summary judgment with the right of trial by jury. *See* Frank T. Boesel, *Summary Judgment Procedure*, 6 Wis. L. Rev. 5, 9-13 (1930).[9] Most of

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[9] Boesel begins his discussion with the following sentence:

> In New York, the question of the constitutionality of this rule arose almost immediately after its adoption, and its validity was vigorously attacked. It was earnestly contended that by applying this rule the

(continued...)

the early, cases upheld summary judgment procedure against constitutional attacks. In *Dwan v. Massarene*, 192 N.Y.S. 577 (ICY. App. Div. 1922), for example, a New York court stated:

> The constitution provides (art. 1, sec. 2): "The trial by jury in all cases in which it has been heretofore used shall remain inviolate forever." It secures the right to a jury trial of the issues of fact in those cases where it had been theretofore used. This did not deprive the court of the power to determine whether there was an issue of fact to be tried; but if the court determined there was such an issue, it must be tried by a jury. A false denial interposed for the purpose of delay did not create such an issue, any more than a false affirmative defense.

Dwan, 192 N.Y.S. at 581, quoted in *Boesel, supra* note 1, at 9.

76. In reviewing these early cases, one is struck by the caution with which courts addressed the constitutional issue. Courts defended summary judgment on the narrow grounds that judges should have the power to strike out sham or frivolous pleas, *Eisele & King v. Raphael*, 101 A. 200, 201 (ICJ. 1917); *Towne v. Dunn*, 136 N.W. 562, 563 (Minn. 1912), and avoid unnecessary delay. Summary judgment was less encompassing then than it is today; even so, judicial opinions usually voiced allegiance to the principle that juries should decide disputed facts and juries should pass on credibility.

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[9] (...continued)
defendant was deprived of his constitutional right to a trial by jury, as provided for by the New York Constitution.

Frank T. Boesel, *Summary Judgment Procedure*, 6 Wis. L. Rev. 5, 9 (1930).

77. In his law review article advocating that Wisconsin adopt a summary judgment rule or statute, Frank Boesel acknowledged that "the ascertainment and determination of what is and what is not a real bona fide defense presents the most difficult problem in [summary judgment's] application and administration." *Boesel, supra* note 1, at 17.

> Each case must, of course, be considered on its own particular facts and circumstances, and in disposing of each case presented to the court, little, if any, assistance will be derived from any attempts to apply general rules or principles. It would appear, however, that if there is any doubt whatever in the mind of the court as to the existence of such a bona fide issue, it should be resolved in favor of the defendant, and the matter determined only after a hearing or trial in the regular order. This is particularly true where a square question of credibility of witnesses arises . . . .

Id.

78. In Wisconsin there are many cases that describe summary judgment as "a drastic remedy." For example, in *Lecus v. Am. Mut. Ins. Co. of Boston*, 81 Wis. 2d 183, 260 N.W.2d 241 (1977), the court said: "We have often stated summary judgment is a drastic remedy and should not be granted unless the material facts are not in dispute, no competing inferences can arise, and the law that resolves the issue is clear. Summary judgment is not to be a trial on affidavits and depositions." *Id.* at 189.

79. As Justice Heffernan observed in *Village of Fontana-on-Geneva Lake v. Hoag*, 57 Wis. 2d 209, 203 N.W.2d 680 (1973), "summary judgment is a drastic remedy which, if granted, deprives the parties of a trial." *Id.* at 214. His opinion

went on to express concern about a litigant being "deprived of his constitutional right to try the issues of fact." *Id.*

80. The *Lecus* case stands for the additional proposition that the issue of intent is not one that properly can be decided on a motion for summary judgment, *Lecus*, 81 Wis. 2d at 190, and this principle is not dead. Similarly, the court of appeals has stated that "Summary judgment should not be granted where the resolution of a dispositive issue depends on state of mind." *Hudson Diesel v. Kenall*, 194 Wis. 2d 531, 547, 535 N.W.2d 65 (1995) (citing *Gouger v. Hardtke*, 167 Wis. 2d 504, 517, 482 N.W.2d 84 (1992)).

81. In the rush to move cases along, summary judgments can be abused. Summary judgments will not be constitutionally suspect so long as courts faithfully limit them to situations in which material facts are not in dispute, intent and state of mind are not at issue, and the credibility of witnesses is not material. As Justice Sykes clearly demonstrates, that is not the situation here.

82. This is a tort case involving an insurer's alleged breach of duty of good faith in dealing with its insured. *See* Wis. JI–Civil 2761. The plaintiff was required to prove, among other things, that there was no reasonable basis for the insurance company to deny its claim. The case is more difficult than a traditional bad faith case because the policy issued by the insurance company did not contain hired and non-owned coverage, as the insured requested. Hence, Tower must have grappled with questions of whether it had to reform its policy and had to pay damages, or whether liability would be assumed or shared by the negligent insurance agent's errors and omissions insurance carrier.

83. Despite this situation, Circuit Judge Marianne Becker found every element of the tort of bad faith by the insurer to be

beyond dispute. Our court of appeals disagreed, but this court overrules the court of appeals' determination that material facts were in dispute and insists that no inferences helpful to the insurer could have been drawn from the facts. This is breathtaking. Surely, we have come a long way from the days when this court said that on summary judgment a court does not try the issues but only decides whether there is an issue for trial. *Wis. Tel. v. Cent. Contracting*, 254 Wis. 480, 483, 37 N.W.2d 24 (1949).

84. What the majority decision seems to ignore is that the tort of bad faith is inextricably linked to the punitive damages issue that went to the jury. At trial, Tower Insurance was not able to defend itself on a level playing field. The circuit court left handprints on the scales of justice by taking the bad faith issue from the jury and *instructing* the jury as to the defendant's bad faith.

85. The plaintiff was a church, the defendant was an insurance company, and the judge was making official pronouncements about the defendant's bad faith. Is there any wonder that the jury awarded $3,500,000 in punitive damages?

86. This case may be precedent for generations to come. The procedure we ratify is wrong, even if the result can be defended.

87. DIANE S. SYKES, J. (dissenting). I respectfully dissent. I agree with the court of appeals that the circuit court's sua sponte order granting summary judgment to Trinity on its bad faith claim was improper. The tort of bad faith is an intentional tort. *Anderson v. Continental Ins. Co.*, 85 Wis. 2d 675, 691, 271 N.W.2d 368 (1978). "To show a claim for bad faith, a plaintiff must show the absence of a reasonable basis for denying benefits of the policy and the defendant's knowledge or reckless disregard of the lack of a reasonable basis for denying the claim." *Id.*

88. The tort of bad faith contains an objective and a subjective element. *Weiss v. United Fire & Cas. Co.*, 197 Wis. 2d 365, 377, 541 N.W.2d 753 (1995). The first element—the absence of a reasonable basis for denying the claim–is objective. *Id.* at 378. The second element—the defendant's knowledge or reckless disregard of the absence of a reasonable basis for denying the claim—is subjective. *Id.* at 392. The "subjective component can be inferred from a 'reckless disregard of a lack of a reasonable basis for denial or a reckless indifference to facts or to proofs submitted by the insured.'" *Id.* (quoting *Anderson*, 85 Wis. 2d at 693).

89. Issues of subjective intent are generally not suitable for resolution on summary judgment. *Tri-Tech Corp. of America v. Americorp Serv.*, Inc., 2002 WI 88, 130 n.5, 254 Wis. 2d 418, 646 N.W.2d 822. "We have stated [that] the issue of intent is not one that properly can be decided on a motion for summary judgment. Credibility of a person with respect to his subjective intent does not lend itself to be determined by affidavit." *Lecus v. American Mut. Ins. Co. of Boston*, 81 Wis. 2d 183, 190, 260 N.W.2d 241 (1977) (citing *Doern v. Crawford*, 30 Wis. 2d 206, 214, 140 N.W.2d 193 (1966)); *see also Green Spring Farms v. Spring Green Farms Assoc.*, 172 Wis. 2d 28, 41, 492 N.W.2d 392 (Ct. App. 1992).

90. Here, Tower moved for summary judgment on the bad faith claim, arguing that it had a reasonable basis to deny Trinity's coverage claim as a matter of law. Trinity opposed the motion, arguing that there was no reasonable basis to deny the claim (because it was entitled to reformation of the policy) and that there were disputed issues of material fact regarding Tower's knowledge or reckless disregard, requiring a jury trial. The circuit court denied Tower's motion, but then, pursuant to Wis. Stat. § 802.08(6), sua sponte entered summary judgment for Trinity. The parties eventually stipulated to compensatory damages in the amount of $17,570, representing the reasonable value of the attorneys' fees Trinity had incurred in proving up insurance coverage. The case proceeded to trial on the issue of punitive damages only.

91. The court of appeals concluded that summary judgment was inappropriate because "the facts related to what Tower actually knew and thus whether there was intentional disregard are in dispute." *Trinity Evangelical Lutheran Church v. Tower Ins. Co.*, 2002 WI App 46, ¶21, 251 Wis. 2d 212, 234, 641 N.W.2d 504. The majority correctly notes that this misstates the intent component of the bad faith tort, which requires "knowledge or reckless disregard of the lack of a reasonable basis for denying the claim" rather than "intentional disregard" as stated by the court of appeals. *Anderson*, 85 Wis. 2d at 691; majority op., ¶37. However, later in its opinion, the court of appeals reframes the disputed issue as "whether the facts necessary to evaluate the claim were properly investigated and developed or recklessly ignored and disregarded," or alternatively, whether there was a "knowing failure to exercise an honest and informed judgment." *Id.*, ¶¶25, 27. This correctly states the subjective intent component of the bad faith tort.

92. Because issues of subjective intent are generally not amenable to resolution on summary judgment— particularly summary judgment entered sua sponte—I agree with the court

of appeals that summary judgment on the bad faith claim was improperly granted. The circuit court's written decision on summary judgment notes that "[Gene] Gallagher [Tower's vice president] testified that he did not actually know whether Trinity had requested non-owned and hired auto insurance." Decision on Motion for Summary Judgment, July 21, 1999, p. 7. Nevertheless, the circuit court concluded that Gallagher's failure to contact the underwriter Fischer (who testified that he had actual knowledge), consult with legal counsel, or contact Trinity satisfied the subjective knowledge element of bad faith under *Anderson*. Decision on Motion for Summary Judgment, p. 8.

93. While the evidence cited by the circuit court strongly supports a finding of reckless disregard, Tower was entitled to have a jury decide the matter after a trial rather than have the circuit court do so on the basis of a paper record. Evaluating issues of knowledge or recklessness involves weighing credibility and drawing inferences, a task for a jury at trial, not a court on summary judgment. Although it was not entitled to summary judgment in its favor on the objective element of the tort of bad faith (the absence of a reasonable basis to deny the claim), Tower was entitled to litigate at least the subjective element at a jury trial.

94. This is especially true in light of the claim for punitive damages, which was tried on the basis of instructions that informed the jury that the court had determined "as a matter of law" and as a result of "undisputed material facts" that Tower had "acted in bad faith in denying coverage to Trinity because, A, Tower lacked a reasonable basis for denying coverage to Trinity . . . and, B, based on Tower's failure to conduct an adequate investigation of Trinity's claim for coverage, Tower recklessly failed to ascertain that coverage to Trinity . . . should have been provided." As a result of the summary judgment, Tower was precluded from presenting evidence or argument that it was not guilty of bad faith— either the objec-

tive or the subjective components of the claim. Instead, the jury was told that Tower's bad faith was an established matter, not open to dispute, and that it need only decide whether Trinity was entitled to punitive damages.

95. Accordingly, I do not agree with the majority's decision to reverse the court of appeals and reinstate the circuit court's grant of summary judgment. I would affirm the court of appeals' decision to the extent that it reversed and remanded for trial on Trinity's bad faith claim.

96. Although the court of appeals reversed the circuit court's order of summary judgment on the bad faith claim, it nevertheless upheld the jury's $3.5 million award of punitive damages. The majority affirms this part of the court of appeals' opinion. I do not agree.

97. Any punitive damages claim is necessarily interwoven in the underlying determination of liability or fault. This is particularly true in the intentional tort of bad faith, for which liability attaches only upon a determination of the defendant's knowing or reckless disregard of the rights of the plaintiff. Here, the entry of summary judgment eliminated Tower's ability to present evidence that it did not possess the requisite level of intent to establish liability for the intentional tort upon which any award of punitive damages would necessarily be premised. The starting point for the jury was the fact that Tower's bad faith had already been conclusively established. The circuit court instructed the jury that bad faith and reckless disregard had been determined by the court as a matter of law on the basis of "undisputed material facts," which necessarily influenced the jury's consideration of the appropriateness and amount of punitive damages. For this reason alone, I would reverse the award of punitive damages.

98. In addition, however, the punitive damages award cannot withstand the due process test for excessiveness established in *BMW of North America v. Gore*, 517 U.S. 559, 575 (1996), which requires a reviewing court to evaluate, de novo, 1) the degree of reprehensibility of the conduct; 2) the disparity or ratio between the punitive damages award and the harm or potential harm suffered; and 3) the difference between the punitive damages award and any civil or criminal penalties authorized for the conduct.[1] *See also Cooper Industries v. Leatherman Tool Group*, 532 U.S. 424, 431 (2001).

99. The United States Supreme Court has very recently reaffirmed the *BMW* test and the requirement of de novo review: "Exacting appellate review ensures that an award of punitive damages is based upon an 'application of law, rather than a decisionmaker's caprice.'" *State Farm Mut. Auto. Ins. Co. v. Campbell*, 538 U.S. ___, 123 S.Ct. 1513, 1520-21 (2003), (citing *Cooper Industries*, 532 U.S. at 436, quoting in turn *BMW*, 517 U.S. at 587 (Breyer, J., concurring)).

100. *Campbell*, like this case, was a bad faith cause of action against an insurance company. The issue was whether "an award of $145 million in punitive damages, where full compensatory damages are $1 million, is excessive and in

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[1] While the majority applies a de novo standard of review (as it must under *Cooper Industries v. Leatherman Tool Group*, 532 U.S. 424 (2001)), it shows some potential for confusion by citing certain language from *Jacque v. Steenberg Homes, Inc.*, 209 Wis. 2d 605, 626, 563 N.W.2d 154 (1997): "[w]e are reluctant to set aside an award merely because it is large or we would have awarded less." Majority op., ¶46. De novo review requires independent evaluation by the reviewing court, which may indeed result in a substitution of the reviewing court's opinion for that of the jury, contrary to the quoted language in *Jacque*.

violation of the Due Process Clause of the Fourteenth Amendment to the Constitution of the United States." *Id.* at 1517. The Supreme Court invalidated the $145 million punitive damages award, concluding that it "was neither reasonable nor proportionate to the wrong committed," and that it was "an irrational and arbitrary deprivation of the property of the defendant." *Id.* at 1526.

101. Under both *BMW* and the Supreme Court's recent decision in *Campbell*, de novo review of the degree of reprehensibility of the defendant's conduct depends in part on whether the conduct was violent, caused physical injury, or was "purely economic," and whether it involved "trickery and deceit" or something closer to mere negligence. *BMW*, 517 U.S. at 575-76; *Campbell*, 123 S.Ct. at 1521. Exemplary or punitive damages "should reflect 'the enormity of [the] offense.'" *BMW* at 575. In *Campbell*, the Supreme Court elaborated:

> We have instructed courts to determine the reprehensibility of a defendant by considering whether: the harm caused was physical as opposed to economic; the tortious conduct evinced an indifference to or a reckless disregard of the health or safety of others; the target of the conduct had financial vulnerability; the conduct involved repeated actions or was an isolated incident; and the harm was the result of intentional malice, trickery, or deceit, or mere accident . . . . The existence of any one of these factors weighing in favor of a plaintiff may not be sufficient to sustain a punitive damages award; and the absence of all of them renders any award suspect.

Campbell, 123 S. Ct. at 1521.

102. None of these factors is present here. The conduct at issue implicated economic injury only (insurance coverage), and, in fact, Trinity was never at risk of having no insurance at all; either the agent's insurance carrier would provide coverage, or Tower would, depending upon the outcome of the coverage dispute. Also, Tower provided legal counsel and a defense as soon as Trinity was sued, and ultimately stipulated to reformation and paid the underlying claim. No one was physically injured; no one's health or safety was at risk. Nor was there any financial vulnerability, for the reasons just noted. There was no intentional malice, trickery, or deceit.

103. The majority characterizes Tower as a "recidivist" for purposes of evaluating the reprehensibility of its conduct, citing the fact that Tower was the defendant in *Trible v. Tower Ins. Co.*, 43 Wis. 2d 172, 168 N.W.2d 148 (1969). Majority op., ¶¶59-60. By no stretch of the facts or imagination can Tower be considered a "recidivist" on the basis of *Trible*.

104. In *Trible*, this court held that an insurance agency's mistake is attributable to the insurer under agency law, and that reformation is an appropriate remedy for mutual mistake in an application for insurance. *Trible*, 43 Wis. 2d at 181-84. Yes, Tower was the defendant in *Trible*, but it was not a bad faith case; it was an action on an insurance contract, and in affirming the circuit court's reformation of the policy we noted that there had been a factual dispute on the issue of mistake, which had been resolved by the factfinder in favor of the insured. *Trible*, 43 Wis. 2d at 180. Contrary to the majority's assertions, then, majority op., ¶59, *Trible* did not hold that Tower had violated any duty, disregarded any law, or otherwise committed bad faith against its insured. Tower can hardly be considered a "repeat offender"on the basis of Trible.

105. "[P]erhaps [the] most commonly cited indicium of an unreasonable or excessive punitive damages award is its ratio to

the actual harm inflicted on the plaintiff." *BMW*, 517 U.S. at 580. Punitive damages "must bear a 'reasonable relationship' to compensatory damages." *Id.* Here, $3.5 million in punitive damages was awarded on the basis of only $17,570 in compensatory damages, a very steep 200:1 ratio.

106. Without even mentioning this 200:1 ratio of punitive damages to actual compensatory damages in this case, the majority, like the court of appeals, seems to adopt (although this is not entirely clear) Trinity's position that there is only a 7:1 ratio between the punitive and compensatory damages, citing evidence of "a harm" of $490,000. Majority op., ¶65. The $490,000 figure represents Trinity's liability in the underlying auto accident, but that amount has no bearing on the actual or even potential compensatory damages in the bad faith claim. As noted above, Trinity was never at risk for the auto accident damages, because either the agent (that is, his errors and omissions carrier) or Tower was responsible for the mistake in the insurance application. The actual compensatory damages in the bad faith claim consisted of the attorneys fees Trinity incurred in the coverage dispute, not the personal injury damages in the underlying lawsuit, which Trinity would not and did not have to pay.[2]

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[2] In discussing the standard of review, the majority notes that in *Management Computer Services v. Hawkins, Ash, Baptie & Co.*, 206 Wis. 2d 158, 557 N.W.2d 67 (1996), this court faulted the circuit court for setting forth only "conclusory reasons " and failing to "analyze the evidence" on a punitive damages issue. Majority op., ¶48. The majority makes the same mistake here in its evaluation of the second *BMW* factor. It says that "Tower introduced evidence that the only potential damage in this case was $17,000." Majority op. ¶65. Actually, the $17,570 figure definitively represents the actual—not "potential"—compensatory damages in this case.

(continued...)

107. The majority recognizes that due process requires a comparison of punitive damages to compensatory damages, and that "[c]ompensatory damages represent the actual harm inflicted on the plaintiff." Majority op., ¶63. Inexplicably, the majority fails to undertake the proper comparison (punitive damages to actual compensatory damages) and instead endorses (apparently) an improper comparison of punitive damages to a measure of "potential harm" that has no relationship to the bad faith claim upon which the punitive damages award was premised. As noted above, there was no "potential" that Trinity would have to pay the claimant in the underlying lawsuit, because either the insurance agent or Tower would be required to do so depending upon the result of the coverage litigation. In any event, a comparison of punitive damages to a creative (but obviously inapplicable) measure of "potential harm" is entirely inappropriate where, as here, actual compensatory damages have in fact been determined. Indeed, the jury was instructed that the compensatory damages were $17,570 and that punitive damages may be awarded based upon that amount of compensatory damages. The majority's position, apparently adopting Trinity's, amounts to nothing more than a manipulation of the ratio for purposes of due process scrutiny.[3]

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[2] (...continued)
The majority then notes that "Trinity introduced evidence of a [potential] harm of $490,000" and goes on to conclude that "[t]he punitive damages award represents a 7:1 ratio of punitive damages to compensatory damages, *if* Trinity's position is applied." *Id.* (emphasis added). Apparently the majority is adopting "Trinity's position," although it does not say so directly (there is the qualifier "if"), and it gives no reasons for doing so.

[3] The Supreme Court reiterated in *State Farm Mut. Auto. Ins. Co. v. Campbell*, 538 U.S. ___, 123 S.Ct. 1513, 1520 (2003), (continued...)

108. The majority's approach to this second *BMW* factor is also directly at odds with *Campbell*. There, the Supreme Court compared the punitive damages award to the actual compensatory damages in the bad faith action, not the damages in the underlying auto accident litigation. *Campbell*, 123 S. Ct. at 1524.

109. The Supreme Court also stated in *Campbell* that it is now an established principle in the law of punitive damages that "few awards exceeding a single-digit ratio between punitive and compensatory damages . . . will satisfy due process." *Id.* at 1524. The Court, having declared that the case was "neither close nor difficult," held that the 145:1 ratio of punitive-to-compensatory damages in *Campbell* could not pass constitutional muster. *Id.* at 1522, 1526. Particularly in light of this most recent pronouncement from the Supreme Court, the 200:1 punitive-to-compensatory damages ratio in this case clearly exceeds constitutional limits.

110. The third factor of the *BMW* analysis requires a comparison of the punitive damages award to any "civil or criminal penalties that could be imposed for comparable

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[3] (...continued)
that "[t]he Due Process Clause does not permit a State to classify arbitrariness as a virtue. Indeed, the point of due process—of the law in general—is to allow citizens to order their behavior. A State can have no legitimate interest in deliberately making the law so arbitrary that citizens will be unable to avoid punishment based solely upon bias or whim." The Court also stated that "[t]he principles set forth in *Gore* must be implemented with care, to ensure both reasonableness and proportionality." *Id.* at 1525-26. The majority's summary and vague apparent adoption of Trinity's position lacks the clarity of analysis required by the de novo due process review the Supreme Court has mandated.

misconduct." *BMW*, 517 U.S. at 583. The majority notes that the court of appeals dismissed this factor as "largely irrelevant " because the court had concluded that the "legislature has not prescribed penalties for the type of conduct engaged in by the defendant." Majority op., ¶167 (quoting *Trinity*, 2002 WI App 46, 141).

111. The majority goes on to note that the legislature has in fact provided a criminal penalty, including a fine of up to $10,000, for any violation of "any insurance statute or rule of this state," Wis. Stat. § 601.64(4), and that the Wisconsin Administrative Code contains insurance rules that prohibit unfair settlement practices, including the " [f]ailure to attempt in good faith to effectuate fair and equitable settlement of claims submitted in which liability has become reasonably clear." Wis. Admin. Code § Ins. 6.11 (3) (a) (4) (Jan. 2002). Majority op., ¶68. This statute and rule proscribe conduct that is comparable to the tort of bad faith. The $3.5 million punitive damages award in this case, evaluated against the $10,000 maximum fine provided for in Wis. Stat. § 601.64(4), yields a 350:1 ratio, even more startling than the 200:1 ratio for punitive-to-compensatory damages. In *Campbell*, the Supreme Court said it "need not dwell long on this [BMW] guidepost" because the applicable $10,000 state fine for comparable conduct was "dwarfed by the $145 million punitive damages award." *Campbell*, 123 S. Ct. at 1526. The same is true here.[4]

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[4] The majority cites certain language from Campbell regarding the third *BMW* factor, but it does so incompletely. Majority op., ¶66. After indicating in *Campbell* that a criminal penalty may have "less utility" when used to determine the amount of punitive damages, the Supreme Court went on to emphasize that "[g]reat care must be taken to avoid use of the civil process to assess criminal penalties that can be imposed only after the heightened protections of a criminal trial have

(continued...)

112. Our own precedent also requires that this punitive damages award be reversed. In *Management Computer Services v. Hawkins, Ash, Baptie & Co.*, 206 Wis. 2d 158, 196, 557 N.W.2d 67 (1996), this court held that a punitive damages award of $1.75 million on a compensatory damages award of $65,000 "is shocking to the conscience of the court." Applying the *BMW* test, particularly the requirements that punitive damages bear a reasonable relationship to compensatory damages and possible criminal penalties for comparable misconduct (there, as here, $10,000), and noting that the case (like this one) involved economic injury only, this court concluded that the $1.75 million punitive damages award "is excessive and therefore a violation of due process, because it is more than is necessary to serve the purposes of punitive damages." *Management Computer Servs.*, 206 Wis. 2d at 196.

113. It is true that there is no "mathematical bright line between the constitutionally acceptable and the constitutionally unacceptable" for purposes of comparing punitive damages to compensatory damages or comparable civil or criminal penalties. *BMW*, 517 U.S. at 583. *Management Computer Services*' 30:1 ratio of punitive to compensatory damages and 175:1 ratio of punitive damages to comparable criminal penalties was "shocking to the conscience of the court" and excessive to the point of violating due process. *Management Computer Servs.*,

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[4] (...continued)
been observed, including, of course, its higher standards of proof. Punitive damages are not a substitute for the criminal process, and the remote possibility of a criminal sanction does not automatically sustain a punitive damages award." *Campbell*, 123 S. Ct. at 1526. As this additional language from the decision makes clear, the Court in *Campbell* was cautioning against using the existence of an applicable criminal penalty as grounds to sustain a punitive damages award, not the converse.

206 Wis. 2d at 196. I can find no principled way to reach a different conclusion in this case, which presents a 200:1 ratio of punitive to compensatory damages and a 350:1 ratio of punitive damages to comparable criminal penalties.

114. Accordingly, I would reverse the court of appeals' decision to the extent that it upheld the award of punitive damages in this case, and remand the entire matter for a new trial on bad faith liability as well as punitive damages.

115. I am authorized to state that Justices JON P. WILCOX and DAVID T. PROSSER JR. join this dissent.

COURT OF APPEALS
DECISION
DATED AND FILED

January 30, 2002

Cornelia G. Clark
Clerk of Court of Appeals

NOTICE

This opinion is subject to further editing. If published, the official version will appear in the bound volume of the Official Reports. A party may file with the Supreme Court a petition to review an adverse decision by the Court of Appeals. See WIS. STAT. § 808.10 and RULE 809.62.

Appeal No. 01-1201
Cir. Ct. No. 98-CV-108

STATE OF WISCONSIN
IN COURT OF APPEALS
DISTRICT II

TRINITY EVANGELICAL LUTHERAN CHURCH AND SCHOOL-FREISTADT, PLAINTIFF-RESPONDENT,

V.

TOWER INSURANCE COMPANY,
DEFENDANT-APPELLANT.

APPEAL from a judgment of the circuit court for Waukesha County: DONALD J. HASSIN, Judge. *Reversed and cause remanded with directions.*

Before Brown, Anderson and Snyder, JJ.

1. ANDERSON, J. Tower Insurance Company (Tower) appeals the judgment in favor of its insured, Trinity Evangelical Lutheran Church and School-Freistadt (Trinity), entered on a jury's verdict finding that punitive damages attached to a bad faith finding made by the trial court and awarding punitive damages in the amount of $3,500,000. Tower's principal contentions are that the trial court erred in granting summary judgment for Trinity on the issue of bad faith and erred as a matter of law by submitting punitive damages to the jury. Tower additionally contends that the punitive damages verdict was not obtained through a fair process and that the ends of justice warrant a new trial. Finally, Tower argues that the punitive damages verdict violates due process and Wisconsin public policy. We conclude that the trial court erred in granting summary judgment for Trinity on the issue of bad faith and remand for a trial on whether Tower's actions constitute bad faith.

Background

2. Trinity is comprised of a church and school located in Mequon, Wisconsin. The school services approximately 234 grade school children and employs eight teachers. Trinity owns property and real estate but does not own any automobiles. Prior to 1994, Trinity was insured by Heritage Insurance through Hackbarth Insurance Service, Inc. in Milwaukee, Wisconsin. Trinity carried hired and non-owned automobile insurance coverage because the teachers for Trinity occasionally, in the course of their employment, transported students to and from certain functions. The policy with Heritage was scheduled for renewal on February 10, 1994.

Facts

3. In 1994, prior to the renewal of the Heritage policy, Trinity decided to get renewal quotations from other insurance carriers. Trinity dealt directly with Jim Rodrian at Rodrian and Associates, Inc. when obtaining an insurance quote. Because Trinity owned no vehicles, it informed Rodrian that it wanted hired and non-owned automobile coverage as part of its liability policy. Rodrian and Associates is an independent insurance agent that does business with, among others, Tower. Rodrian has an executed agency agreement with Tower, whereby Tower authorized Rodrian to "receive, accept and, in accordance with the Company's binding guidelines, bind proposals for contracts of insurance for risks located in Wisconsin." Rodrian requested a coverage quote for Trinity from Tower. He dealt with Harold Fischer, an underwriter at Tower. He provided Fischer with basic information regarding the risk, and passed on information regarding quotes given to Trinity from other insurance carriers. In addition to discussing other coverage with Fischer, Rodrian told Fischer that Trinity wanted hired and non-owned automobile coverage on the policy. Rodrian received a quote from Fischer that Rodrian believed included the hired and non-owned automobile coverage requested. Rodrian provided this information to Trinity. Trinity accepted Tower's quote. Fischer authorized Rodrian to bind coverage on behalf of Tower.

4. On February 10, 1994, Rodrian forwarded a pre-application binder to Trinity that included coverage for hired and non-owned automobiles. After the binder was sent to Trinity, the application was filled out for the issuance of the policy. Inadvertently, Rodrian failed to check the box requesting hired and nonowned insurance coverage on the application. Tower subsequently issued a policy to Trinity without the hired and non-owned coverage. None of the parties or participants spotted the error at that time.

5. On January 24, 1995, Lorrie Erdman, a teacher at Trinity, while transporting students from the school in the course of her employment, ran a stop sign and collided with another vehicle. The collision resulted in serious injuries to the other vehicle's driver and passenger.

6. Trinity notified Rodrian of the potential claim. Upon review of the policy, Rodrian discovered that there was not any hired and non-owned automobile vehicle coverage indicated. In a letter to Carol Blackwell, a district manager in Tower's underwriting department, dated January 31, 1995, Rodrian informed Tower of the accident and of the fact that he had mistakenly failed to request hired and non-owned automobile coverage on the application. He requested that Tower backdate Trinity's coverage.

7. In response to Rodrian's letter, Blackwell drafted a memo to Gene Gallagher, the vice president and director of operations at Tower. Blackwell's memo recapped the circumstances surrounding Rodrian's error and asked for direction as to how to handle Rodrian's request to backdate coverage.

8. Within twenty-four to forty-eight hours, Gallagher instructed Blackwell to tell Rodrian that Tower would not backdate Trinity's coverage. It is Trinity's position that Gallagher did nothing to investigate Tower's duty to Trinity before making his decision and that this non-investigation among other things constituted bad faith on Tower's part. Trinity points out that Gallagher made his decision without ever contacting Tower's in-house attorney for advice on the matter and without ever contacting Trinity to verify Rodrian's representation.

9. Gallagher's decision was memorialized in a handwritten note to Blackwell:

> Carol-Your referral says that this is agency error and not ours. We didn't get request to provide [hired and non-owned coverage] didn't get copy of binder till now, so [we] don't have any reason to backdate. Suggest agent [Jim Rodrian] alert his E and O carrier if he hasn't already. I'm not going to put backdate and add with uncertainty as to possible exposure. We could be facing big dollars due to liab[ility]?? If you want to discuss further let me know. Gene

Thereafter, Blackwell met with Rodrian on February 2, 1995, to inform him of Tower's decision.

10. After its decision, Gallagher and Tower were asked on numerous occasions to reconsider. Notably, one of these requests for reconsideration came in the form of a letter mailed to Gallagher by Jim Reynolds, the adjuster at Rodrian's Errors and Omissions (E&O) carrier (J. Soukup & Co., Inc., an insurance claim investigation and adjustment firm). This letter included a case law citation to *Trible v. Tower Insurance Co.*, 43 Wis. 2d 172, 168 N.W.2d 148 (1969) (the lead case instructing when a claim for reformation of an insurance policy is warranted). Gallagher did not read the case. Tower did not change its decision.

11. Three years after the accident, the involved parties began filing suit. Tower undertook the representation of Trinity under a reservation of rights. Tower retained counsel to represent Trinity on the issue of liability. Tower also retained its own attorney, Arnold Anderson. On May 18, 1998, Tower, through Anderson, filed a motion for summary judgment asking to be dismissed as a party in the case entirely. Tower stated that "the contract of insurance it issued to Trinity does not cover the claims stated in the complaint. Specifically, the policy does not cover claims arising out of the operation of a motor vehicle."

Tower did not conduct discovery prior to filing the motion for summary judgment. Tower requested summary judgment solely on the basis of the language of the written policy. Its motion did not bring to the court's attention that it had been informed by its agent that the written policy was in error, that its agent had requested that the policy be backdated, and that it had denied its agent's request for backdating.

12. In response to Tower's motion for summary judgment, Trinity hired an attorney to represent it on the question of insurance coverage and filed an action for reformation and breach of contract. Shortly thereafter, Tower withdrew its motion for summary judgment.

13. On September 28, 1998, Trinity deposed Fischer, the Tower underwriter who dealt with Rodrian in regard to Trinity's policy. During the course of Fischer's deposition, Trinity discovered that in June 1995, four months after Blackwell had met with Rodrian to inform him of Tower's decision, an investigator hired by Rodrian had tracked down Fischer and obtained a signed statement from him verifying that Rodrian had indeed asked Fischer to include hired and non-owned automobile coverage in Trinity's policy. Two days after Trinity deposed Fischer, Tower stipulated to reform Trinity's policy to include non-owned and hired coverage at the time of the accident. Tower also paid approximately $490,000 to discharge Trinity's liability in its entirety in the underlying accident suit.

14. Tower's stipulation to reform Trinity's policy and its payout to discharge Trinity's liability did not settle the controversy. Given the information provided by Fischer, Trinity amended its cross-claim to assert a bad faith cause of action against Tower. In response, Tower filed a motion for summary judgment seeking dismissal of the bad faith claim. In its written decision on Tower's motion, the trial court determined that Trinity was entitled to reformation of the insurance policy as a

matter of law. The trial court further concluded that Tower's conduct constituted bad faith under the standard set forth in *Anderson v. Continental Insurance Co.*, 85 Wis. 2d 675, 691, 271 N.W.2d 368 (1978), and accordingly granted summary judgment for Trinity pursuant to WIS. STAT. § 802.08(6) (1999-2000).[1]

15. Subsequent to the trial court's decision, the only factual issue left for determination by the jury was whether punitive damages attached. After hearing several days of testimony, including testimony from Gallagher that he had no knowledge of: principal/agency law, the law of reformation, Wisconsin's Unfair Claims Practices Act, nor Trible, the jury determined that Tower had acted "in an intentional disregard of the rights of the plaintiff" awarding $3,500,000 in punitive damages to Trinity. Tower's numerous motions after verdict were denied and judgment was entered on the verdict on March 15, 2001. It is from this final judgment that Tower appeals.

Law and Analysis

16. At the outset, we note that an analysis on reformation is not necessary because that issue has been settled in the lower court. Tower agreed to reform the policy; additionally, the trial court held that as a matter of law, Tower had to reform the policy.

Bad Faith

17. First we will dispose of Tower's argument that bad faith cannot exist in the context of reformation. Tower cites *Combined Investigative Services, Inc. v. Scottsdale Insurance Co.*,

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[1] All references to the Wisconsin Statutes are to the 1999-2000 version unless otherwise noted.

165 Wis. 2d 262, 270-71, 477 N.W.2d 82 (Ct. App. 1991), and *Kranzush v. Badger State Mutual Casualty Co.*, 103 Wis. 2d 56, 60-62, 307 N.W.2d 256 (1981), to support its argument that Wisconsin has not recognized bad faith claims in reformation cases. Tower contends that the trial court improperly expanded the scope of bad faith liability in the reformation context. We do not agree.

18. *Combined* and *Kranzush* explain that claims for bad faith have generally been limited to (1) an injured's action against the tortfeasor's insurer; (2) an insured's action against its own insurer's handling of its claim under a casualty, life, health, or accident policy; and (3) a third party's action against the insurer for failure to reimburse a worker's compensation claim. *Combined*, 165 Wis. 2d at 269-70; *Kranzush*, 103 Wis. 2d at 60-62. Trinity's bad faith action falls into the second accepted category. Trinity's cross-claim for bad faith is an insured's action against its own insurer's handling of its claim under an accident policy. *Kranzush*, 103 Wis. 2d at 61. Thus, contrary to Tower's assertion, the trial court did not expand the tort of bad faith into other areas of the law in its recognition of Trinity's bad faith claim.

19. Nonetheless, we conclude that the trial court erred when it granted summary judgment in favor of Trinity on the issue of bad faith. When reviewing a grant of summary judgment, we apply the standards set forth in WIS. STAT. § 802.08, just as the trial court applies those standards. *Voss v. City of Middleton*, 162 Wis. 2d 737, 748, 470 N.W.2d 625 (1991). Under § 802.08(2), summary judgment must be entered "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." Our first step in the summary judgment methodology is to discern whether the pleadings set forth a claim for relief as well as a material issue

of fact. *Grams v. Boss*, 97 Wis. 2d 332, 338, 294 N.W.2d 473, (1980). If the pleadings meet this initial test and our review of the record shows that the moving party has made a prima facie case for summary judgment, we examine the record to discern whether there "exist[s] disputed material facts, or undisputed material facts from which reasonable alternative inferences may be drawn, sufficient to entitle the opposing party to a trial." *Id.*

20. In the present case, the pleadings of Tower set forth a claim for relief as well as material issues of fact. Tower alleged in its complaint that Trinity's claim of bad faith was without merit; that Tower had a reasonable basis to deny claims arising out of the underlying accident; and finally, that Tower did not breach any contractual duty and was not negligent in any way. Tower also alleged a variety of facts to support its three reasons for summary judgment. Therefore, Tower has overcome the first hurdle in the summary judgment analysis.

21. Our analysis now shifts to whether there existed any disputed material facts. Both Tower and Trinity contend that there are disputed facts and while they each do so at self-serving junctures in the timeline of this case,[2] our review of the record confirms that a dispute existed and summary judgment was inappropriate. Trinity claimed (in its brief in opposition to Tower's motion for summary judgment on the bad faith issue) that there existed material issues of fact that ought to go to a jury. Trinity argued, "Tower misrepresents the facts when it claims that, prior to the commencement of the lawsuit, Trinity did not request reformation nor present any evidence to

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[2] Trinity argues that there are disputed facts in its trial brief in opposition to Tower's motion for summary judgment on Trinity's bad faith claim. Tower, on appeal and with the knowledge that the trial court granted summary judgment against it on the bad faith issue, agrees with Trinity that there are facts in dispute.

establish entitlement to reformation." Trinity claimed that Tower's argument that Trinity did not request reformation or present any evidence to establish entitlement to reformation requires a factual finding from the court regarding what information was known by or available to Tower immediately after the automobile accident in January 1995. Trinity requested that the court leave it to a jury, in its role as fact finder, to determine the facts surrounding Tower's knowledge at the time of denial. On appeal, Tower renews Trinity's assertion that there existed disputed facts which precluded summary judgment, stating, "Trinity also argued that there was ample evidence precluding Tower's motion for summary judgment, and that the bad faith issue should be left to the jury." We agree with the parties that the facts related to what Tower actually knew and thus whether there was intentional disregard are in dispute. We therefore find that there were material facts in dispute, making summary judgment inappropriate.

22. Because the bad faith issue should have been left to the jury, our bad faith discussion is meant to assist the parties and the trial court on remand. Wisconsin's law on an insurer's duty to avoid bad faith is well developed.

> [I]n every insurance contract there is an implied covenant of good faith and fair dealing. The duty to so act is imminent in the contract whether the company is attending to the claims of third persons against the insured or the claims of the insured itself. Accordingly, when the insurer unreasonably and in bad faith withholds payment of the claim of its insured, it is subject to liability in tort.

Anderson, 85 Wis. 2d at 689. By entering into an insurance contract and taking control of settlement or litigation, the insurer assumes a fiduciary duty on behalf of the insured.

Prosser v. Leuck, 225 Wis. 2d 126, 138, 592 N.W.2d 178 (1999). Because the insured has given up something of value to the insurer—namely, the right to defend and settle a claim—the insurer has been said to be in the position of a fiduciary with respect to an insured's interest in settlement of a claim. *Id.*

23. The fiduciary duty "carries with it the duty to act on behalf of the insured and to exercise the same standard of care that the insurance company would exercise were it exercising ordinary diligence in respect to its own business." *Id.* The fiduciary duty imposes several obligations on the insurer. This includes the duty to diligently investigate to ascertain facts upon which to base a good faith decision whether to settle. *Id.* The insurer must fulfill this obligation as part of its fiduciary duty even if it challenges coverage. *Id.* at 139.

24. In order to succeed on a claim of bad faith, the insured must show (1) an absence of a reasonable basis for denying the policy benefits and (2) the insurer's knowledge or reckless disregard of the lack of a reasonable basis for denying the claim. *Anderson*, 85 Wis. 2d at 691. An absence of a reasonable basis for denying the claim exists when the claim is not fairly debatable. *Mowry v. Badger State Mut. Cas. Co.*, 129 Wis. 2d 496, 516, 385 N.W.2d 171 (1986). Once again, in applying this test, it is appropriate to determine "whether a claim was *properly investigated* and whether the results of the investigation were subjected to a reasonable evaluation and review." *Anderson*, 85 Wis. 2d at 692 (emphasis added). Recently, the supreme court reiterated this mandate in *Danner v. Auto-Owners Ins.*, 2001 WI 90, 245 Wis. 2d 49, 629 N.W.2d 159. In *Danner*, the insured sued her underinsured carrier, claiming failure to exercise good faith in the investigation, evaluation and processing of a claim. *Id.* at ¶2. The insurer asked the court to narrowly interpret the good faith duty to investigate, arguing that there can be no bad faith claim against

a UIM carrier for the investigation, evaluation or processing of a claim until arbitration established the company's legal obligation to pay. *Id.* at ¶43. The court rejected this argument, holding that every insurance contract from its inception has an implied covenant of good faith and fair dealing between the insured and insurer. *Id.* at ¶57.

25. However, when a claim is "fairly debatable," the insurer is entitled to debate it. *Drake v. Milwaukee Mut. Ins. Co.*, 70 Wis. 2d 977, 984, 236 N.W.2d 204 (1975). In *Drake*, it was determined that "there was a genuine dispute over the status of the law at the time the denials were made, and it cannot be said that the company's denials were made in bad faith." *Id.* It is apparent then that the insurer is entitled to debate a fairly debatable claim regardless of whether the debate concerns a matter of fact or law. Nonetheless, the tort of bad faith can be alleged only if the facts pleaded would, on the basis of an objective standard, show the absence of a reasonable basis for denying the claim, i.e., would a reasonable insurer under the circumstances have denied or delayed payment of the claim under the facts and circumstances. *Anderson*, 85 Wis. 2d at 692. So whether a claim is "fairly debatable" additionally implicates the question of whether the facts necessary to evaluate the claim were properly investigated and developed or recklessly ignored and disregarded. *Id.* at 691.

26. The law of reformation which obliges the insurance company to reform a contract where the insured has shown by clear and convincing evidence that there was a mutual mistake in the policy is unquestioned. *See Trible*, 43 Wis. 2d at 182. Under no view of the applicable law is an insurer's reformation obligation "fairly debatable." The trial court found that a mutual mistake occurred and that reformation was in order. Tower does not appeal this finding. Moreover, Tower had already agreed to reform the policy before the trial court held that it was

obligated to do so. What is at issue is whether Tower acted in bad faith prior to its acquiescence to reform.

27. The tort of bad faith is an intentional one. *Anderson*, 85 Wis. 2d at 691. "Bad faith" by definition cannot be unintentional. Id. Bad faith is the absence of honest, intelligent action or consideration based upon knowledge of the facts and circumstances upon which a decision in respect to liability is predicated. *Id.* at 692. There is a duty of ordinary care and reasonable diligence on the part of an insurer in handling claims, and the knowing failure to exercise an honest and informed judgment constitutes bad faith. *Id.* In short, it is proper when applying the bad faith test, to determine whether a claim was properly investigated and whether the results of the investigation were subjected to a reasonable evaluation and review; this will be the jury's task on remand.

Punitive Damages

28. With regard to the punitive damages award, we uphold the award *if* on remand the jury finds bad faith. We recognize that in order to discuss our decision to uphold the punitive damages award we must assume arguendo that bad faith was properly found. Our analysis will reflect the assumption that bad faith exists. However, if the jury *does not* find bad faith, the punitive damages award is nullified.

29. Proof of a bad faith cause of action does not necessarily make punitive damages appropriate. *Id.* at 697. There is a distinction between the intent necessary to maintain an action for bad faith and the intent that must be shown to recover punitive damages. *Id.* For punitive damages to be awarded in addition to compensatory damages for the tort, there must be a showing of an evil intent deserving of punishment or of something in the nature of special ill-will or wanton disregard of duty or gross or outrageous conduct. *Id.*

30. Tower argues that the trial court erred as a matter of law by submitting punitive damages to the jury. Before the question of punitive damages in a tort action can properly be submitted to the jury, the trial court must determine, as a matter of law, that the evidence will support an award of punitive damages. *Jacque v. Steenberg Homes, Inc.*, 209 Wis. 2d 605, 614, 563 N.W.2d 154 (1997). A question on punitive damages may not be given to the jury unless the trial court concludes that a reasonable jury could find from the evidence that entitlement to punitive damages has been proven by clear and convincing evidence. *Lievrouw v. Roth*, 157 Wis. 2d 332, 344, 459 N.W.2d 850 (Ct. App. 1990). Whether there is sufficient evidence to submit a punitive damages question to the jury is a legal matter that an appellate court must determine independently. *Id.* "The plaintiff may receive punitive damages if evidence is submitted showing that the defendant acted maliciously toward the plaintiff *or in an intentional disregard* of the rights of the plaintiff." WIS. STAT. § 895.85(3) (emphasis added). The law requires that we view the evidence in a light most favorable to the jury's verdict. *Fehring v. Republic Ins. Co.*, 118 Wis. 2d 299, 305-06, 347 N.W.2d 595 (1984), *overruled on other grounds by DeChant v. Monarch Life Ins. Co.*, 200 Wis. 2d 559, 547 N.W.2d 592 (1996). Upon our independent review of the record, we hold that Trinity supplied credible evidence to show that Tower acted in an intentional disregard of Trinity's rights; this showing is enough to support the submission of punitive damages to the jury.

31. Tower additionally contends that the punitive damages verdict was not obtained through a fair process and that the ends of justice warrant a new trial. This contention is based on Tower's belief that the trial court erred in allowing Trinity to present to the jury improper opinion testimony of economist Robert Niendorf. Tower claims that Niendorf included Tower's parent company's (Atlas) finances in assessing what amount Tower could afford to pay in punitive damages. Tower says

that under Wisconsin law, punitive damages cannot be based on the assets of a nonparty parent corporation. We need not verify this because, for our purposes, even assuming Tower has stated Wisconsin law correctly, contrary to Tower's assertion, Niendorf's testimony did not include improper information about Tower's parent company.

32. Niendorf's testimony was admitted via videotape deposition. From our reading of his testimony, it did not inform the jury of the financial resources of Atlas. The trial court redacted any reference to Atlas's assets from Niendorf's testimony before it was presented to the jury. Niendorf's testimony did not reference the financial wealth of Atlas. It does not appear that Niendorf's theories regarding Tower's ability to pay relied on the financial well-being of Atlas. And finally, each source of money listed as available to satisfy a punitive damages judgment was totally internal to the financial assets of Tower. We hold that the process was untainted by Niendorf's testimony.

33. Finally, Tower argues that the punitive damages verdict violates due process and Wisconsin public policy. Punitive damages may properly be imposed to further a state's legitimate interests in punishing unlawful conduct and deterring its repetition. *BMW of N. Am., Inc. v. Gore*, 517 U.S. 559, 568 (1996). The award of punitive damages in a particular case is entirely within the discretion of the jury. *Jacque*, 209 Wis. 2d at 626. However, we apply a de novo standard of review when passing on a trial court's determination of the constitutionality of punitive damages awards. *Cooper Indus., Inc. v. Leatherman Tool Group, Inc.*, 121 S. Ct. 1678, 1685-86 (2001). Only when an award can fairly be categorized as "grossly excessive" in relation to the state's interests in punishment and deterrence does it enter the zone of arbitrariness that violates due process. *Jacque*, 209 Wis. 2d at 627. The test for "gross excessiveness" stems from an elementary notion of fairness that a party receive

fair notice not only of the conduct that will subject it to punishment, but also of the severity of the penalty that a state may impose. *BMW*, 517 U.S. at 574. The test has three parts: (1) the degree of reprehensibility of the conduct, (2) the disparity between the harm or potential harm suffered and the punitive damages award, and (3) the difference between the punitive damages and the possible civil or criminal penalties imposed for the conduct. *Id.* at 575.

34. Thus, we focus first on the scope of the state's legitimate interests in punishing Tower and deterring it from future misconduct. *See id.* If we find that the punitive damages award accomplishes these interests, we then turn to the factors in the *BMW* test and weigh them against the state's interest in punishment and deterrence. *See Jacque*, 209 Wis. 2d at 627.

35. As an insurance company in Wisconsin, Tower has an implied duty of good faith and fair dealing and our law has developed such that this duty encompasses the obligation to investigate disputed coverage claims. *Prosser*, 225 Wis. 2d at 138. The state has a legitimate interest in deterring Tower from burying its proverbial head in the sand only to later claim ignorance of what this duty entails. We find that the $3,500,000 dollar punitive damages award against Tower well serves the legitimate interest of punishment and deterrence. Certainly Tower will feel the effect of this sanction, but that is the point of punishment. Moreover, as a result of this punishment, Tower will very likely become schooled in its duty as an insurer in order to protect itself from making the same costly mistake in the future.

36. Because we find that the punitive damages award accomplishes the legitimate state interests of punishment and deterrence, we now weigh the factors in the *BMW* test against these interests. *See Jacque*, 209 Wis. 2d at 627. We turn first to the reprehensibility factor. "The most important indicium of

the reasonableness of a punitive damage award is the degree of reprehensibility of the defendant's conduct." *Id.* at 628. In addressing the reprehensibility of Tower's conduct, it is appropriate to consider evidence that suggests that Tower engaged in prohibited conduct while knowing or suspecting that it was unlawful. *See BMW*, 517 U.S. at 576. And if this is the case, then strong medicine is required to cure this type of disrespect for the law. *Id.* at 576-77. Punitive damages should reflect the egregiousness of the offense. *Jacque*, 209 Wis. 2d at 628.

37. Bear in mind that when we review the record to determine whether a punitive damages award is excessive, the evidence must be viewed in the light most favorable to the plaintiff, and a jury's punitive damages award will not be disturbed unless the verdict is so clearly excessive as to indicate passion and prejudice. *Id.* at 626-27. Thus, when viewing the evidence in this light, the offense in this case was Tower's intentional disregard of its duty to diligently investigate to ascertain facts and circumstances underlying the accident upon which to base a good faith decision to settle or determine coverage. *See Prosser*, 225 Wis. 2d at 138.

38. Gallagher's decision to deny coverage within twenty-four to forty-eight hours without knowing whether Trinity had actually requested hired and non-owned automobile coverage and without contacting Trinity to determine this shows an intentional disregard to Tower's insured. Gallagher's decision not to seek the available in-house legal counsel regarding Rodrian's requests for backdating shows a reckless disregard toward Tower's insured. Gallagher's decision not to contact Fischer, Tower's own underwriter with whom Rodrian worked on the Trinity policy, about whether he understood Trinity to have requested hired and non-owned coverage shows a reckless disregard of Trinity in the face of its agent's representation that Trinity had requested coverage. Tower's decision to

send its attorney to the court and ask for summary judgment without ever informing the court of the dispute regarding Rodrian's error and request for backdating shows blatant disrespect for its insured and the court. We have no trouble finding that the reprehensibility factor has been met under *BMW*.

39. We now turn to the second factor: the disparity between the harm or potential harm suffered by Trinity and the punitive damages award. *Jacque*, 209 Wis. 2d at 628-29. When compensatory damages are awarded, we consider the ratio of the compensatory to punitive damages. *Id.* at 629. This is so because compensatory damages represent the actual harm inflicted on the plaintiff. *Id.* Wisconsin law expressly rejects the use of a fixed multiplier, either a fixed ratio of compensatory to punitive damages or of criminal fine to punitive damages, to calculate the amount of reasonable punitive damages. *Id.* However, in the appropriate case, a comparison of the compensatory damages and the punitive damages award is important. While a constitutional line ought not be marked by a simple mathematical formula, the proportionate rule for punitive damages is one factor in determining the reasonableness of the punitive damages award. *Id.*

40. At trial, both parties were given the opportunity to introduce evidence and argue on this issue. Tower introduced evidence that the only potential damage in this case was $17,000; Trinity introduced evidence of a potential harm of $490,000 had Tower succeeded in its summary judgment requesting to be dismissed entirely from the case.[3] The punitive damages award represents a 7:1 ratio of punitive damages to

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[3] We note again that it was stipulated between the parties prior to trial that the total payments made to the injured parties, along with attorneys' fees incurred in the defense of the action, amounted to $490,000.

compensatory damages accepting Trinity's position. We cannot say that this is an unreasonable or constitutionally impermissible award. *See id.* at 626-27.

41. Finally, we turn to the third factor: a comparison of the punitive damages award and the civil or criminal penalties that could be imposed for comparable misconduct. *Id.* at 630. We find this factor "largely irrelevant" to the case at hand. *See id.* The legislature has not put into place a criminal or civil statute prohibiting insurance carriers from intentionally disregarding the contractual rights of an insured and rejecting claims on the basis of their own economic self-interest. Thus, as our supreme court held in *Jacque*, when a legislature has not prescribed penalties for the type of conduct engaged in by the defendant, this third guidepost becomes immaterial. *Id.*

42. Having examined the state's legitimate interests in punishing Tower and deterring it from future misconduct along with the factors in the *BMW* test, if the jury finds bad faith on remand, we uphold the jury's verdict awarding Trinity punitive damages in the amount of $3,500,000.

By the Court.—Judgment reversed and cause remanded with directions.

Recommended for publication in the official reports.

STATE OF WISCONSIN CIRCUIT COURT
WAUKESHA COUNTY
BRANCH 10

WARREN, et al, Plaintiffs, v. Riemer, et al, Defendants.

vs.

RATHER, et al, Plaintiffs, v. American Family Insurance Group, et al, Defendants.

DECISION ON MOTION
FOR SUMMARY JUDGMENT

CONSOLIDATED CASES
Case No. 98-CV-0183
Case No. 98-CV-0108

FILED
in Circuit Court
Jul 21 1999
Waukesha Co. Wis.
Civil Division

FACTS AND PROCEDURAL HISTORY

On January 24, 1995, Defendant Laurie Riemer was involved in an auto accident while driving her vehicle on the business of her employer, Trinity Evangelical Lutheran Church and School ("Trinity"). Some of the occupants of the other vehicle sued Trinity's insurer, Tower Insurance Company ("Tower"). Previously, on February 10, 1994, James Rodrian, an agent of Tower pursuant to an agency agreement, had bound

Trinity's insurance-policy with Tower. Rodrian sent a policy binder to Trinity, which reflected that the policy included, at Trinity's request, non-owned and hired insurance.

When notified of the claim, Rodrian discovered that the non-owned and hired auto insurance box on the application for insurance had not been checked. On January 31, 1995, Rodrian wrote about this situation to Carol Blackwell, District Manager of Tower's Underwriting Department, and requested that the coverage be backdated, i.e., reformed. Blackwell forwarded a memorandum to Gene Gallagher, Vice President of Tower Insurance, which included Rodrian's request for backdated coverage.

Gallagher testified that he denied Rodrian's request because Rodrian, alone, made the mistake by not checking the non-owned and hired box and that Tower did not receive a copy of the binder within three days of Rodrian's issuance of the binder to Trinity. Again, in April 1995, Rodrian wrote to Tower and coverage was still denied by Gallagher. Since the discovery process commenced for this action, Tower has reformed the policy to include non-owned and hired auto insurance.

Trinity cross-claimed that Tower acted in bad faith by not reforming its insurance policy and thus, denying its claims arising out of the auto accident.

Tower now moves for summary judgment, claiming that it had a reasonable basis to deny Trinity's claims.

ANALYSIS

There are four issues in this case: (1) whether Trinity was entitled to reformation of its insurance policy with Tower at the time Rodrian requested reformation; (2) whether Tower acted

in bad faith by denying reformation and coverage to Trinity; (3) whether summary judgment is appropriate in this case; and (4) whether attorney's fees are appropriate in this case.

A. REFORMATION

A claim for reformation of an insurance policy is permissible when "the [party] seeking reformation shows that because of . . . mutual mistake, the policy does not contain provisions desired and intended to be included. *Trible v. Tower Insurance. Co.*, 43 Wis. 2d 172, 182 (1969), followed by *Scheideler v. Smith & Associates, Inc.*, 206 Wis. 2d 480, 486 (Ct. App. 1996). The burden of proof necessary to show that a mutual mistake was made on the insurance policy application is that of clear and convincing evidence. *Jewell v. United Fire & Casualty Co.*, 25 Wis. 2d 509, 516-17 (1964). Mutual mistake exists when "the insured makes statements to an agent concerning coverage and the agent understands but, by mistake, causes a policy to be issued that does not contain the requested coverage." *Trible* at 182. If the agent made the mistake and is an authorized agent of the insurer, the mistake is attributable to the insurer for reformation of the contract. *Id.* at 181-82. *See also* Wis. Stat. 628.40 1998.

Tower argues that it had a reasonable basis to deny Trinity's claims arising out of the accident because the insurance policy between Tower and Trinity did not cover non-owned and hired auto insurance. While it is true that the insurance application did not reflect the existence of non-owned and hired insurance, such coverage had existed ever since Rodrian agreed to provide the coverage.

A mutual mistake occurred when Rodrian did not check the non-owned and hired auto insurance box on the insurance application, but understood that Trinity had requested that coverage. *Trible* at 181. There was an understanding between

Trinity and Rodrian that the policy through Tower was to include non-owned and hired auto insurance. (Rodrian Dep. at 18-21; Jaskulski Aff., Exs. P, Q.) Also, Harry Fischer, a senior underwriter at Tower with whom Rodrian worked on Trinity's policy, testified that Rodrian wanted to attain non-owned and hired auto insurance for Trinity. (Rodrian Dep. at 18-21; Fischer Dep. at 9, 23-24; Jaskulski Aff., Ex. H.)

Second, through Rodrian, Trinity showed by clear and convincing evidence that there was a mutual mistake in the policy. *Trible* at 182; *Jewell, supra*, at 516-17. As this Court earlier held, Rodrian, as Tower's authorized agent, solely made the mistake of not checking the non-owned and hired auto insurance box on the insurance application. When Rodrian discovered the error, he wrote letters to Tower, which reached Gallagher, communicating that he erred in filling out the application and requesting that the policy be reformed to include non-owned and hired auto insurance. (Gallagher Dep. at 7-9; Jaskulski Aff., Exs. P, Q, R.) Trinity's burden of demonstrating that a mutual mistake existed in the formation of the policy was concededly[4] satisfied when Rodrian, on behalf of *Trinity*, requested reformation of the policy. (Gallagher Dep. at 68-69.)

Third, since Rodrian, as an authorized agent, made the mistake, the mistake is attributable to Tower in reformation of the insurance policy. *Trible* at 181; Wis. Stat. § 628.40 (1998). Contrary to Tower's assertion, the non-owned and hired auto coverage legally existed at the time the policy was originally put in place. As the Wisconsin Supreme Court stated, "[When] the facts warrant such reformation . . . [the court] is not making a new contract for the parties, but it is making a new writing to express the actual intended contract of the parties. "*Langer v.*

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[4] i.e., conceded by Gallagher.

Stegerwald Lumber Co., 262 Wis. 383, 390 (1952). Consequently, when Rodrian originally requested reformation of Trinity's insurance policy, the requirements for reformation were satisfied and Trinity was entitled to reformation.

B. BAD FAITH

In order to succeed on a claim of bad faith, Trinity must show (1) an absence of a reasonable basis "for denying the policy benefits and (2) Defendant's "knowledge or reckless disregard of the lack of a reasonable basis for denying the claim." *Anderson v. Continental Insurance Co.*, 85 Wis. 2d 675, 691 (1978). Also, an absence of a reasonable basis for denying the claim exists when the claim is not fairly debatable. *Mowry v. Badger State Mutual Casualty Co.*, 129 Wis. 2d 496, 516 (1986). In applying this test, it is appropriate to determine "whether a claim was properly investigated and whether results of the investigation were subjected to a reasonable evaluation and review. *Anderson* at 692. Moreover, an insurer has a duty to "diligently investigate to ascertain facts and circumstances underlying the accident upon which to base a good-faith decision" to settle or determine coverage. *Prosser v. Leuck*, 225 Wis. 2d 126, 138 (1999), citing *Mowry*, *supra*, at 510; *Mowry* at 524. The insurer "must fulfill [this] obligation as party of its fiduciary duty . . . if it challenges coverage." *Mowry* at 524, followed by *Prosser*, *supra*, at 139.

Citing *Combined Investigative Services, Inc. v. Scottsdale Insurance Co.*, Tower argues that Wisconsin has not recognized bad faith claims in reformation cases. *See Combined*, 165 Wis. 2d 262, 270 (Ct. App. 1991). Moreover, Tower argues that if this Court recognizes the instant bad faith claim, it is expanding the tort of bad faith into other areas. (Brief of Defendant in Support of Summary Judgment at 15.)

This Court does not agree. Neither the *Combined* court nor the *Kranzush* court to which *Combined* cites uses the word "reformation." *See Kranzush v. Badger State Mutual Casualty Co.*, 103 Ws. 2d 56 (1981). The *Combined* and *Kranzush* courts do say, however, that claims for bad faith have generally been limited to (1) an injured's action against the tortfeasor's insurer; (2) an insured's action against its own insurer's handling of its claim under a casualty, life, health, or accident policy; and (3) a third party's action against the insurer for failure to reimburse a worker's compensation claim. *Combined* at 269-270; *Kranzush* at 60-62. This Court finds that Trinity's bad faith action falls into the second accepted category. Trinity's cross-claim for bad faith is "an insured's action against its own insurer's handing of its claim under a[n] . . . accident policy." *Kranzush* at 60-62. Contrary to Tower's assertion, this Court is *not* expanding the tort of bad faith into other areas of the law by recognizing Trinity's bad faith claim.

The next stage in the bad faith analysis is to decide (1) whether Tower had a reasonable basis for denying reformation and thus, denying coverage to Trinity and (2) whether Tower had knowledge of the lack of reasonable basis for denying the claim. *Anderson* at 691. Tower lacked a reasonable basis for denying reformation of Trinity's insurance policy.

Blackwell received and read letters from Rodrian requesting reformation and forwarded a memo regarding this issue to Gallagher. (Blackwell Dep. at 10-13.) Gallagher knew of and had read Rodrian's requests for reformation. (Gallagher Dep. at 6-9, 67-69.) Jim Reynolds, the adjuster at Rodrian's E&O carrier (J. Souk up & Co., Inc., an insurance claim investigation and adjustment firm), even mailed Gallagher a letter, which included case law citations, requesting that Gallagher "honor and adjust" the claim. (Jaskulski Aff., Ex. R).

Moreover, Gallagher never "properly investigated" the reformation claim before he denied it the first and second times. *Anderson* at 692. Gallagher testified that he did not actually know whether Trinity had requested non-owned and hired auto insurance. (Gallagher Dep. at 95-96, 99.) Even though he did not know whether Trinity had coverage, Gallagher never sought legal counsel regarding Rodrian's requests during the time of the requests for reformation on behalf of Trinity, even though he had in-house counsel at his disposal. (*Id.* at 75-76.) Gallagher never contacted the insured to see if Trinity had requested the non-owned and hired coverage. (*Id.*) Gallagher never contacted Harry Fischer, with whom Rodrian worked on the Trinity policy, about whether Trinity wanted non-owned and hired coverage. (*Id.* at 77, 99, 113-15.) In fact, throughout Gallagher's deposition, he testified that he had several opportunities to revisit the non-owned and hired coverage issue, but he decided to deny the reformation based on his beliefs about Trinity's coverage.

The manner in which Tower denied the reformation requests constituted bad faith pursuant to the *Anderson* court. The claim for reformation that determines, as a matter of law, whether Trinity was covered by non-owned and hired auto insurance at the time of the accident in question, was not "fairly debatable" because of Tower's failure to properly investigate the reformation request, *Anderson* at 691, as this record clearly reflects. Without knowledge as to whether Trinity was covered under its policy, Gallagher did not seek legal counsel and did not contact the Tower underwriter who worked with Rodrian to see if Trinity actually requested non-owned and hired auto coverage. Instead of seeking counsel and probing into the coverage question, Gallagher simply denied reformation because coverage was not requested on the insurance application. With virtually no investigation, Tower did not make a reasonable investigation, thus the claim was not "fairly debatable," and Tower did not have a reasonable basis for denying

the claim. *Id.* at 691-92. Further, through Fischer, Blackwell, and Gallagher, the record reflects that Tower had knowledge of the intended coverage and also had knowledge that it did not properly investigate the reformation requests. Therefore, because this Court finds that the lack of reasonable basis and knowledge requirements of Anderson are satisfied, Tower acted in bad faith in denying reformation of Trinity's insurance policy.

C. SUMMARY JUDGMENT

Summary judgment is appropriate when "there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." *Peters v. Menard, Inc.*, 224 Wis. 2d 174, 191-92 (1999), citing *Verdoljak v. Mosinee Paper Corporation*, 200 Wis. 2d 624, 630 (1996). *See also* Wis. Stat. § 802.08(2) (1998). Although there is no genuine issue of material fact in the instant case, Tower, as the moving party, is not entitled to judgment as a matter of law. As a matter of law, Trinity was entitled to reformation of its insurance policy with Tower at the time Rodrian requested reformation on its behalf. Further, as a matter of law and contrary to Tower's assertions, Tower acted in bad faith by denying Trinity reformation, i.e. coverage under Trinity's policy.

D. ATTORNEY'S FEES

Tower argues that Trinity's cross-claim is a reformation action and that therefore, coverage did not exist and attorney's fees are not warranted. (Brief of Defendant in Support of Summary Judgment at 20-21.) Because Trinity was entitled to reformation, the non-owned and hired insurance had existed from the time the policy was bound. Although the law of reformation is important to this case, Trinity's cross-claim is a bad faith claim against Tower for not reforming and thus,

covering the accident pursuant to the insurance policy. The Supreme Court of Wisconsin has recently stated that "when an insurer acts in *bad* faith by denying benefits, it is liable to the insured in tort for any damages which are the proximate result of that conduct." *DeChant v. Monarch Life Insurance Co.*, 200 Wis. 2d 559, 571 (1996).

In *DeChant*, a bad faith action, the court found insurance claims that were paid untimely proximately caused and forced the insured to hire an attorney to obtain the benefits. *Id.* at 571. The *DeChant* court went on to state that "[u]nless *DeChant* is able to obtain relief in the form of attorney's fees and other damages, the bad faith denial of his policy benefits will expose him to numerous uncompensable harms." *Id.* at 577. This case is analogous to *DeChant*. Because Tower did not properly investigate the claim for reformation, Trinity was "forced" to hire its own counsel to prove that they were entitled to reformation and thus, that coverage actually existed. In other words, the absence of investigation proximately caused Trinity to hire counsel. Attorney's fees are warranted in this case.

CONCLUSION

From the inception of Trinity's insurance policy with Tower, Trinity was legally covered by non-owned and hired auto insurance. The policy was entitled to reformation based on Rodrian's mistake in filling out the application and his request on Trinity's behalf to have the policy reformed. Tower acted in bad faith by not investigating or not properly investigating the reformation request while knowing that such an investigation should have been performed. Attorney's fees are proper in this case because Tower proximately caused Trinity to hire its own counsel. Finally, Tower is not entitled to summary judgment as a matter of law and therefore, Defendant's motion for summary judgment is **DENIED**. Pursuant to Wis. Stat. 802.08(6),

Plaintiff is entitled to summary judgment; therefore, summary judgment is **GRANTED** to **Plaintiff**.

DATED AT WAUKESHA, WISCONSIN, THIS _21st__ DAY OF JULY, 1999. BY THE COURT:

/s/ Honorable Marianne E. Becker
Honorable Marianne E. Becker,
Circuit Court Judge, Branch 10

<3001>

SUPREME COURT
OF WISCONSIN
OFFICE OF THE CLERK

110 East Main Street, Suite 215
P.O. BOX 1688
MADISON, WISCONSIN 53701-1688
TELEPHONE: (608) 266-1880
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CLERK

Date: July 01, 2003

To:

Edward M. Crane
Skadden, Arps, Slate,
Meagher & Flom
333 West Wacker Drive,
Suite 2100
Chicago, IL 60606

Charles F. Smith
Skadden, Arps, Slate,
Meagher & Flom
333 West Wacker Drive,
Suite 2100
Chicago, IL 60606

M. Christine Cowles
Borgelt, Powell, Peterson &
Frauen, S.C.
735 N. Water St., #1500
Milwaukee, WI 53202-4188

Merrick R. Domnitz
Domnitz, Mawicke &
Goisman, S.C.
1509 N. Prospect Ave.
Milwaukee, WI 53202-
2323

Barbara A. O'Brien
Borgelt, Powell, Peterson &
Frauen, S.C.
735 No. Water St., #1500
Milwaukee, WI 53202-4188

Robert L. Jaskulski
Domnitz, Mawicke &
Goisman, S.C.
1509 N. Prospect Ave.
Milwaukee, WI 53202-
2323

Anthony J. Skemp
Domnitz, Mawicke &
Goisman, S.C.
1509 N. Prospect Ave.
Milwaukee, WI 53202-2323

R. George Burnett
Liebmann, Conway,
Olejniczak & Jerry
P.O. Box 23200
Green Bay, WI 54305

Robert J. Dreps
LaFollette, Godfrey & Kahn
P.O. Box 2719
Madison, WI 53701

William C. Gleisner III
4230 N. Oakland Ave.
Milwaukee, WI 53211

John W. Markson Jr.
Bell, Gierhart & Moore, S.C.
P.O. Box 53701

The court has entered the following order:

Case No. **01-1201**
Trinity Evangelical v. Tower Insurance Co.
Circuit Court Cast No. 98-CV-108

The court having considered the Motion for Reconsideration filed in the above matter,

IT IS ORDERED that the Motion for Reconsideration is denied, with $50.00 costs.

Docketed
July 08 2003

Cornelia G. Clark
Clerk of Supreme Court

STATE OF WISCONSIN CIRCUIT COURT
WAUKESHA COUNTY

SUZANNE M. RATHER and LARRY RATHER,
Plaintiffs,

LUITTINK MANUFACTURING CO.,
Involuntary Plaintiff,

v.

AMERICAN FAMILY INSURANCE GROUP LORRIE ERDMAN, TRINITY EVANGELICAL LUTHERAN CHURCH AND SCHOOL-FREISTADT, TOWER INSURANCE COMPANY and ST. PAUL FIRE AND MARINE INSURANCE CO.,
Defendants,
and
TOWER INSURANCE COMPANY,
Intervenor Defendant,

TRINITY EVANGELICAL LUTHERAN CHURCH & SCHOOL-FREISTADT,
Third-Party Plaintiff,

v.

JAMES R. RODRIAN, RODRIAN & ASSOCIATES, INC. and UTICA MUTUAL INSURANCE COMPANY,
Third-Party Defendants.

Case No. 98 CV 0108
Code No. 30101
BAD FAITH CASE

EXCERPT OF DEFENDANT TOWER INSURANCE COMPANY'S CONSOLIDATED MEMORANDUM OF LAW IN SUPPORT OF ITS POST-TRIAL MOTIONS FOR DIRECTED VERDICT, JUDGMENT NOTWITHSTANDING THE VERDICT, NEW TRIAL, AND REMITTITUR

Pursuant to §§ 805.14 and 805.15 of the Wisconsin Statutes, Tower Insurance Company ("Tower") respectfully submits this memorandum of law in support of its motions for a directed verdict, for judgment notwithstanding the verdict, for a new trial, or in the alternative, for remittitur.

I. INTRODUCTION

This case involves an insurance coverage dispute between two insurance companies, Tower and Utica Mutual Insurance Company, to determine which one should cover an accident involving a teacher at Trinity Evangelical Lutheran Church ("Trinity"). The dispute arises because James Rodrian, an independent insurance agent, failed to request non-owned and hired auto insurance coverage from Tower on behalf of Trinity in 1994. Under Wisconsin law, Rodrian's admitted mistake placed both Tower and Utica (Rodrian's liability carrier) at risk Tower through a contract reformation theory, and Utica as insurer for Rodrian's professional malpractice. *See Scheidler v. Smith & Assocs., Inc.*, 206 Wis. 2d 480, 485, 557 NW.2d 445, 447 (Wis. Ct. App. 1996) (permitting insured to pursue claims against insurer and agent's liability carrier). Trinity thus filed a cross-suit against Rodrian and Utica, while Tower intervened as a defendant in the underlying accident case.

Utica responded to Trinity's cross-suit by engaging in a comprehensive campaign to shift liability to Tower. Tower, meanwhile, followed Wisconsin law. As soon as the lawsuit was filed, Tower hired lawyers to defend Trinity; and when the

lawsuit was resolved, it paid approximately $490,000 to discharge Trinity's liability in its entirety. *See Newhouse v. Citizens Security Mut. Ins. Co*,. 176 Wis. 2d 824, 837, 501 N.W.2d 1, 6 (Wis. 1993) (under Wisconsin law, insurer facing debatable claim must defend insured while reserving rights; "[t]he best approach is for the insurance company to defend under a reservation of rights."). There has never been any claim that Tower failed to provide an adequate defense to Trinity, or that Tower failed to fully cover Trinity's liability. Further, there was never any risk that Trinity would not be covered by insurance on the accident, either from Tower or from Utica. Indeed, both Gene Gallagher and Carol Blackwell testified that they believed the church certainly would be covered under the Utica policy. Plaintiffs allegations notwithstanding, the record evidence is undisputed: the church was never in danger of not being covered by insurance. Nevertheless, Tower has now been sacked with a $3,500,000 punitive damages judgment—a judgment that appears to be the largest punitive damage award in Waukesha County history. *See Church Wins Insurance Battle*, MILWAUKEE JOURNAL SENTINEL, Dec. 22, 2000 (quoting plaintiffs counsel as stating that $3.5 million punitive award is largest in county history).[1]

This $3.5 million award against Tower—two hundred times the amount of compensatory damages awarded in this case—cannot stand under Wisconsin law, the Wisconsin Constitution, or the United States Constitution. The Court should issue a directed verdict or order a new trial. In the alternative, the Court should issue a remittitur reducing the excessive award to a reasonable amount.

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1 Utica, meanwhile, got off scot-free. It never paid a dime to Trinity, and presumably never paid anything under its liability coverage for Rodrian, either. Rodrian himself also emerged unscathed, despite the fact that it was his admitted mistake that sparked this litigation.

II. SUMMARY OF THE ARGUMENT

The Court erred in *sua sponte* granting summary judgment against Tower on plaintiff s bad faith claim, as the procedure employed by the Court denied Tower notice and an opportunity to respond to the matters before the Court. Moreover, it appears that no court in Wisconsin has ever recognized a bad faith cause of action in a reformation case. By recognizing such a claim here, the Court has single-handedly expanded the tort of bad faith, contrary to established Wisconsin precedent limiting bad faith actions to particular circumstances. Finally, on the merits, summary judgment for plaintiff on bad faith was inappropriate, as there is substantial evidence in the record suggesting that Tower acted reasonably, and not in bad faith, in handling plaintiffs claims. That evidence, much of which is undisputed, entitles Tower—not the insured—to summary judgment on bad faith. In the alternative, to the extent there is any genuine issue of fact concerning bad faith, the Court acted improperly in granting summary judgment for plaintiff. The Court should reverse its summary judgment order on bad faith, and either grant summary judgment for Tower, or conduct a trial on the merits of the bad faith claim.

Even with a bad faith finding, however, the $3.5 million punitive damages verdict in this case cannot stand. First, plaintiff failed to present clear and convincing evidence demonstrating that Tower intentionally disregarded Trinity's rights. Accordingly, the Court should either direct a verdict -in Tower's favor, denying punitive damages, or order a new trial. Second, under Wisconsin law, any punitive damages award must relate directly to the underlying tort of bad faith, not to the contract reformation action. Because Judge Becker's ruling that Tower was liable for the tort of bad faith was based on Tower's allegedly incomplete investigation, any punitive damages award must be based on that tort—and on the underlying evidence for that tort. Accordingly, the additional evidence presented by

plaintiff, which does not relate to the tort of bad faith, was improperly admitted by the Court. Tower is therefore entitled to a directed verdict, judgment notwithstanding the verdict, or a new trial. Third, even assuming *arguendo* that the evidence clearly and convincingly established that Tower intentionally disregarded the insured's rights, the $3.5 million punitive award in this case far exceeds Trinity's compensatory damages, as well as other guidelines set forth by the Supreme Court to govern the constitutionality of punitive awards. The verdict in this case thus violates the due process clause of the Fourteenth Amendment and § 1 of the Wisconsin Constitution. The award should be vacated, or significantly reduced.

Finally, the punitive damages award here is irretrievably tainted by the improper opinion testimony of Robert Niendorf, who included the net worth of Tower's parent company, Atlas, in calculating what monies Tower allegedly had available to pay punitive damages. As Tower established in its motion to bar Niendorf's testimony, reaching into a non-party's coffers to inflate the net worth of a defendant for punitive damages purposes is contrary to Wisconsin law. The Court's response to Tower's motion (striking Niendorf's answers explaining his premise that Atlas could finance Tower's payment, but permitting the conclusion that Tower could therefore pay) failed to cure the fundamental defect in Niendorf's testimony. The punitive award is thus irretrievably infected by error. It should be thrown out, and a new trial should be ordered.

III. THE COURT ERRED IN GRANTING SUMMARY JUDGMENT FOR PLAINTIFF ON THE ISSUE OF BAD FAITH

Under Wisconsin law, a Court should grant summary judgment only "where it is perfectly plain that there is no substantial issue to be tried." *Krause v. Western Cas. & Sur. Co.*, 7 Wis. 2d 18, 21, 95 N.W.2d 757, 758-59 (Wis. 1959);

Wis. Stat. § 802.08(2), stats. "Summary judgment is a drastic remedy which should be used only when there is no substantial issue of fact to be tried; when there are substantial issues of fact to be determined or when there are permissible inferences from undisputed facts which would permit a different result, summary judgment should not be granted." *FDIC v. First Mortgage Investors*, 76 Wis. 2d 151, 153-54, 250 N.W.2d 362, 364-65 mss. 1977).

The Court's order granting summary judgment for plaintiff on its bad faith claim is improper for the following reasons: (1) by granting summary judgment *sua sponte*, the Court acted without the benefit of a fully developed factual record, and without providing adequate notice to Tower; (2) the record evidence, much of it undisputed, establishes that Tower did not act in bad faith (at the very least, that evidence creates a genuine issue of fact as to whether Tower acted in bad faith, if it does not entitle Tower to summary judgment altogether); and (3) by granting summary judgment for plaintiffs, the Court impermissibly expanded the tort of bad faith by recognizing, for the first time, a bad faith cause of action in a reformation context. Accordingly, the Court should vacate its summary judgment ruling, and either grant summary judgment for Tower, or set this matter for trial on the question of bad faith.

A. The Court Improperly Granted Summary Judgment for Trinity *Sua Sponte*, Without Giving Tower Notice or an Opportunity to Present Materials in Opposition to the Motion

The Court granted summary judgment for plaintiff on its bad faith claim *sua sponte*, without a fully developed factual record. Although Tower initially moved for summary judg-

ment, the Court granted judgment for Trinity,[2] but without providing Tower notice or a reasonable opportunity to demonstrate the existence of a genuine issue of material fact. *See* Wis. Stat. § 802.08(2), stats. (summary judgment is appropriate only if "the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law."). Although the Court may grant summary judgment to the nonmoving party, Wis. Stat. § 802.08(6), stats., the Court should first consider all the relevant evidence to determine whether there is a genuine issue of fact.

By not giving Tower notice of its intention to grant summary judgment on plaintiff s bad faith claim, the Court deprived Tower of the opportunity to proffer the evidence demonstrating a genuine issue of material fact on that claim.[3] As such, summary judgment was premature. *See, e.g., Monfils v. Charles*, 216 Wis. 2d 323, 331-32 n.4, 575 N..W.2d 728, 732 n.4 (Wis. Ct. App. 1998) (declining to enter summary judgment for non-moving party because "the facts may not have been fully developed"). *See also, e.g., Hispanics for Fair & Equitable Reapportionment v. Griffin*, 958 F.2d 24, 25 (2d Cir. 1992)

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2 Trinity never moved for summary judgment, and in fact conceded in its brief the existence of issues of fact on the bad faith claim.

3 Under Wisconsin law, bad faith claims present mixed questions of law and fact. *Mowry v. Badger State Mut. Cas. Co*, 129 Wis. 2d 496, 516, 385 N.W.2d 171, 181 (Wis. 1986). Given that all of the factual issues were not fully developed and all of the relevant evidence was not presented to the Court, the Court did not have an opportunity to properly decide the questions of fact presented by the instant case.

("[summary judgment should not be granted . . . unless the losing party has been given an opportunity to demonstrate that there are genuine material issues for trial."); *Fili Moretti Cereali S.P.A. v. Continental Grain Co.*, 563 F.2d 563, 565 (2d Cir. 1977) ("[W]hile it is not inappropriate for a district court to grant summary judgment *sua sponte* where it is clear that a case does not present an issue of material fact . . . such power must be exercised with great caution and with care taken to give the parties an opportunity to present materials in opposition to the motion."); *First Financial Ins. Co. v. Allstate Interior Demolition Corp.*, 193 F.3d 109, 114-115 (2d Cir. 1999) (court may grant summary judgment for nonmoving party provided that party against which summary judgment is granted has had a full and fair opportunity to counter proposition that there is no genuine issue of material fact to be tried).

B. The Record Evidence Establishes that Tower Is Entitled to Summary Judgment on Bad Faith, or Alternatively Creates a Genuine Issue of Fact Requiring a Trial Regarding Whether Tower Acted in Bad Faith

Under Wisconsin law, "[t]o establish a claim for bad faith, the insured 'must show the absence of a reasonable basis for denying benefits of the policy and the defendant's knowledge or reckless disregard of the lack of a reasonable basis for denying the claim." *Weiss v. United Fire & Cas. Co.*. 197 Wis. 2d 365, 377, 541 N.W.2d 753, 757 (Wis. 1995) (quoting *Anderson v. Continental Ins. Co.*, 85 Wis. 2d 675, 691, 271 N.W.2d 368, 376 (Wis. 1978)). The first prong is objective, and requires the insured to establish that a reasonable insurer could not have denied or delayed the claim under the facts and circumstances of the case. *Weiss*, 197 Wis. 2d at 378, 541 NW.2d at 757. The second prong is subjective, and "[t]he subjective component can be inferred from a 'reckless disregard of a lack of a reasonable basis for denial or a reckless indifference to facts or to proofs submitted by the insured." *Id.* at 392,

54 N.W.2d at 762-63 (quoting *Anderson*, 85 Wis. 2d at 693, 271 N.W.2d at 377).

Even under the foregoing test of bad faith, however, an insurance company may still "challenge claims which are fairly debatable and will be found liable only where it has intentionally denied (or failed to process or pay) a claim without a reasonable basis." *Anderson*, 85 Wis. 2d at 693, 271 N.W.2d at 377. The insurer additionally has the right to "exercise its own judgment in determining whether a claim should be settled or contested," although exercise of its judgment "should be accompanied by considerations of good faith." *Mowry v. Badger State Mut. Cas. Co.*, 129 Wis. 2d 496, 510, 385 N.W.2d 171, 178 (Wis. 1986) (quotations omitted).

There is ample evidence in the record establishing that Tower acted reasonably, and not in bad faith, in delaying payment on plaintiff's claim. Tower issued a policy of insurance to Trinity on exactly the terms requested by independent insurance agent Rodrian. Because Rodrian did not request coverage for non-owned or hired automobiles, Tower did not include that coverage in the policy it issued. Indeed, it is undisputed that Rodrian was solely responsible for the error, as he and the insured admit. Moreover, although Tower issued the policy to Trinity in the Spring of 1994, and despite the fact that Trinity's insurance committee included Harry Mueller (who had approximately 40 years' experience in the insurance business, and who explained how important it allegedly was to Trinity to secure the hired/non-owned coverage), *neither Trinity nor Rodrian bothered to confirm that the Tower policy included the hired/non-owned coverage at issue until January of the following year—after the accident occurred.*

Under the circumstances, then, Tower reasonably expected that Rodrian's professional liability carrier would pay for his malpractice, and therefore would cover Trinity's claims.

Indeed, this view was consistent with Wisconsin law, which provides that an insured can pursue remedies against either the insurer for contract reformation, or against the agent's professional liability carrier for malpractice. *See Scheidle*r, 206 Wis. 2d at 485, 557 N.W.2d at 447.[4] Further, as soon as Trinity was sued in connection with the accident, Tower hired Trinity's lawyers and paid for Trinity's defense on the merits. Tower then reformed Trinity's policy to include the requested coverage, and paid the entire amount necessary to resolve the claims against the church. Both as a matter of law and as a matter of fact, Trinity was never without coverage in this case.

Taking into account all of the foregoing facts, Tower—not the insured—is entitled to summary judgment on the bad faith claim. Wisconsin law grants insurers the right to assure themselves of the facts before paying a debatable claim or reforming a policy. From the beginning, Tower challenged in good faith what it believed to be a debatable claim. Under Wisconsin law, this should not subject Tower to bad faith liability. *See, e.g, Anderson*, 85 Wis. 2d at 691, 271 N.W.2d at 376 (when either the law or facts supporting a claim are "fairly debatable," a reasonable insurer is entitled to debate the claim, and doing so is not considered bad faith); *Samuels Recycling Co. v. CNA Ins. Cos.*, 223 Wis. 2d 233, 248-49, 588 N.W.2d

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[4] *Trible v. Tower Ins. Co.*, 43 Wis. 2d 172, 168 N. W. 2d 148 (Wis. 1969), does not change this result. That case holds that an insured can pursue a claim against its insurer for reformation where an agent makes a mistake, *id.* at 184-85, 168 N.W.2d at 155, but (contrary to plaintiffs repeated suggestions at trial) says nothing about whether the insured can also pursue a remedy against the agent for malpractice. Because both remedies are viable (and indeed Trinity pursued both remedies here), *Trible* does not render Tower's belief that Utica could be held liable for the loss "reckless," as required for a finding of bad faith.

385, 391-92 (Wis. Ct. App. 1998) (insurer reasonably delayed defending and indemnifying insured where liability coverage of claim for environmental cleanup costs was fairly debatable until resolved against insurer by Wisconsin Supreme Court). *See also Mills v. Regent Ins. Co.*, 152 Wis. 2d 566, 574, 449 N.W.2d 294, 297 (Wis. Ct. App. 1989) ("The fact that coverage under the policy was ultimately established fails to prove the insurer denied the policy claim in bad faith.").

The case of *Guaranty National Insurance Co. v. George*, 953 S.W.2d 946, 947 (Ky. 1997) is particularly instructive. In that case, the plaintiff procured commercial insurance coverage for a personal truck he used for delivering mail. *Id.* at 947. The independent insurance agent listed the wrong vehicle identification number for the truck on the insurance application, however, and due to the agent's admitted mistake, the wrong truck was listed on the face of the insurance policy. *Id.* at 947, 950. Plaintiff's truck was later involved in an accident, in which a third party died. *Id.* at 947. When the third-party's representatives filed a wrongful death action against plaintiff, the insurer hired counsel to defend plaintiff, but reserved the right to deny coverage under the policy, should the facts have indicated coverage was not bound. *Id.* Plaintiff then sued the insurer, alleging bad faith, and the insurer counterclaimed for a declaration of its rights *Id.* The trial court found that a mutual mistake existed and that the insurance coverage should be equitably reformed. *Id.* After the trial court's ruling, the insurer settled the claim. *Id.* at 948. The Kentucky Supreme Court held that the insurer acted reasonably, and not in bad faith:

> [T]here were legal questions of agency and whether the agent's negligence was a factor in the lack of coverage Though in retrospect these issues may appear clear and undebatable, when there is an ambiguity and suspected material error on the face of a policy that would exclude

> coverage, we do not believe it is bad faith for a party to ask a court to either reform or decline to reform the policy.

Id. at 949.

George is dispositive. Like the insurer in that case, Tower acted reasonably by defending Trinity in the accident litigation, while reserving its right to deny coverage should the facts have indicated the policy did not cover the non-owned vehicle. Like Guaranty National, Tower's conduct certainly "does not meet the threshold or rise to the level required to sustain an action for bad faith." *Id. See also Newhouse*, 176 Wis. 2d at 836-37, 501 N.W.2d at 5-6 (under Wisconsin law, when there is a debatable claim, "[t]he best approach is for the insurance company to defend under a reservation of rights."). S*ee also, e.g., Rumford Prop. & Lab. Ins. Co. v. Carbone*, 590 A.2d 398, 401 (R.I. 1991) (insurer's actions in entering into a nonwaiver agreement to defend an insured, and later questioning coverage or bringing a declaratory judgment action on question of coverage, are seen as "efforts to clarify its rights rather than bad-faith maneuvers"); *Truck Ins. Exch. v. Superior Court*, 59 Cal. Rptr. 2d 529, 534 (Cal. Ct. App. 1996) (if insurer defends underlying action under reservation of rights, and files action for declaration that no duty to defend or indemnify exists, such a determination would allow insurer to withdraw from defense without subjecting insurer to bad faith liability); *Royal Ins. Co. v. Process Design Assocs. Inc.*, 582 N.E.2d 1234, 1239 (Ill. App. Ct. 1991) (where insurer believes policy does not provide coverage, insurer must either defend under reservation of rights, or secure declaratory judgment as to its rights and obligations).

The undisputed evidence requires judgment for Tower under the applicable law. Alternatively, there is at the least a genuine issue as to whether Tower acted reasonably in delaying payment on plaintiffs claim. In either case, the Court erred in granting summary judgment for plaintiff on bad faith. The

Court should now reverse that ruling, and either grant summary judgment for Tower, or else conduct a trial to determine whether Tower acted in bad faith with regard to plaintiffs claims.

C. The Court's Summary Judgment Ruling Ignores Established Wisconsin Law Limiting Bad Faith Claims

Wisconsin courts have recognized the tort of bad faith only in limited circumstances, and on several occasions have refused to expand it to new situations. *See Kranzush v. Badger State Mut. Cas. Co.*, 103 Wis. 2d 56, 60-62, 307 N.W.2d 256, 259-60 (Wis. 1981) (enumerating the three situations in which tort of bad faith applies in insurance context); *Combined Investigative Servs. Inc. v. Scottsdale Ins. Co.*, 165 Wis. 2d 262, 270-71, 477 NW.2d 82-85 (Wis. Ct. App. 1991) (refusing to recognize fourth theory of bad faith recovery). Despite the recognition of bad faith claims in the insurance context, Tower is unaware of any case in Wisconsin or any other state that has recognized a bad faith cause of action in a reformation context. There is simply no authority for extending bad faith liability to reformation cases, and the Court erred in doing so when it granted summary judgment for plaintiff in this matter.

Nor is the unprecedented step of expanding the tort of bad faith to reformation cases justified. Wisconsin law and common sense dictate that bad faith liability should not be imposed on insurance companies until an insured has carried its burden of proving that a policy should be reformed. Because Wisconsin places the burden of proving entitlement to reformation on the insured, *Williams v. State Farm Fire & Casualty Co.*, 180 Wis. 2d 221, 235-36, 509 NW.2d 294, 300 (Wis. Ct. App. 1993), courts cannot require an insurer to reform a policy immediately, based simply on a policyholder's say-so. Moreover, under established Wisconsin law, until an insured has proved his reformation claim, the insurer may rely on the insurance policy

as written. *See Jilek v. Zahl*, 162 Wis. 157, 160, 155 N.W. 909, 910 (Wis. 1916) (contract "may be reformed for mistake and enforced as reformed, but until reformed its provisions are controlling").

The Court's summary judgment ruling runs counter to these established legal principles by effectively requiring Tower to reform Trinity's policy before Trinity had carried its burden of proving the need for reformation. Moreover, by recognizing a bad faith claim in this reformation case, the ruling disregards Wisconsin law that states that a party may rely on the written provisions of a contract until it is reformed. The Court should vacate its summary judgment ruling.

IV. THE PUNITIVE DAMAGES VERDICT SHOULD BE VACATED

Even were the Court's *sua sponte* bad faith summary judgment ruling appropriate,[5] the Court should nevertheless direct a verdict for Tower on the separate question of punitive damages, which is subject to an even more stringent standard of proof than bad faith. In the alternative, the Court should grant judgment notwithstanding the verdict, order a new trial on punitive damages, or issue a remittitur substantially reducing the $3,500,000 award.

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[5] If not vacated by this Court now, this novel summary judgment ruling will be reviewed *de novo* by the Court of Appeals. *See Millen v. Thomas*, 201 Wis. 2d 675, 682, 550 N.W.2d 134, 137 (Wis. Ct. App. 1996) (summary judgment reviewed *de novo*).

A. Because the Punitive Damages Verdict Is Not Supported By Credible Evidence that Tower Intentionally Disregarded Plaintiff's Rights, the Court Should Direct a Verdict for Tower or Order a New Trial

1. New Trial and Directed Verdict Standards

The Court may set aside the verdict and order a new trial "because of errors in the trial, or because the verdict is contrary to law or to the weight of evidence, or because of excessive or inadequate damages, or . . . in the interest of justice." Wis. Stat. § 805.15(1), stats. *See also Meke v. Nicol*, 56 Wis. 2d 654, 664, 203 N.W.2d 129, 135 (Wis. 1973) (trial court erred in failing to set aside entire verdict due to gross disproportion between plaintiffs proven compensatory damages and verdict, coupled with very large award of punitive damages, which was enhanced by admission of erroneous evidence concerning defendant's wealth); Wis. Stat. § 805.15(6), stats. (court may set aside verdict as excessive). A trial court also may order a new trial if evidence was admitted at trial in error. *See Lease America Corp. v. Insurance Co. of N. Am.*, 88 Wis. 2d 395, 402, 276 N.W.2d 767, 770 (Wis. 1979) (new trial warranted where prejudicial effect of testimony outweighed probative value, and evidence therefore was improperly admitted). All of these problems infected the trial in this case.

In addition to ordering a new trial, the Court may direct a verdict for Tower if, viewing the evidence in the light most favorable to Trinity, there is no credible evidence to sustain the punitive award in Trinity's favor. Wis. Stat. § 805.14(1), stats. Accordingly, "taking into consideration all facts and circumstances as they appear in evidence, [if] there is but one inference or conclusion that can be reached by a reasonable man," a directed verdict is appropriate. *Zillmer v. Miglautsch*, 35 Wis. 2d 691, 698-99, 151 N.W.2d 741, 745 (Wis. 1967) (quoting *City of Milwaukee v. Bichel*, 35 Wis. 2d 66, 68, 150 N.W.2d

419, 421 (Wis. 1967)). *See also* Wis. Stat.§ 805.14(5)(d), stats. (renewed motions for directed verdict).

2. Because the Evidence In this Case Does Not Support the Punitive Damages Award, the Court Should Direct a Verdict for Tower, or Order a New Trial

Before a punitive damages request can be submitted to a jury, the Court must determine whether, as a matter of law, the evidence will support a punitive damages award. *Jacque v. Steenberg Homes. Inc.*, 209 Wis. 2d 605, 614, 563 N.W.2d 154, 158 (Wis. 1997). A heightened burden of proof applies to punitive damages claims—plaintiff must prove by clear and convincing evidence that punitive damages are warranted. *See, e.g., Carlson & Erickson Builder, Inc. v. Lampert Yards. Inc.*, 190 Wis. 2d 650, 659, 529 N. W.2d 905, 908 (Wis. 1995). "The plaintiff may receive punitive damages if evidence is submitted showing that the defendant acted maliciously toward the plaintiff or in an intentional disregard of the rights of the plaintiff." Wis. Stat. § 895.85(3), stats. The punitive damages standard ("intentional disregard") is thus even higher than the bad faith standard ("reckless disregard").[6]

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[6] In 1995, the Wisconsin legislature enacted a new statute, Wis. Stat. §895.85, which revised the law of punitive damages in Wisconsin. According to the Wisconsin Civil Jury Instructions Committee, the new statute, by instituting the "intentional disregard" standard, was clearly intended to be more narrow than the previous case law standard which had allowed recovery of punitive damages for *reckless* indifference to or disregard for the rights of others. *Unified Catholic Schools of Beaver Dam Educational Ass'n v. Universal Card Servs. Corp.*, 34 F. Supp. 2d 714, 718 (E.D. Wis. 1999); Wis. JI-Civil 1707 n.2.

There is no evidence, and Trinity does not even allege, that Tower acted maliciously in this case. Indeed, it is undisputed that Tower bore no ill will towards Trinity. Rather, plaintiff's sole contention is that Tower intentionally disregarded its rights. Even viewed in the light most favorable to plaintiff, however, the record evidence does not demonstrate "clearly and convincingly" that Tower intentionally disregarded Trinity's interests. Rather, the following facts are undisputed:

- Tower immediately hired lawyers for Trinity, and paid for Trinity's entire defense, as soon as Trinity was sued in connection with the accident;

- Tower reformed Trinity's policy and paid the entire amount necessary to resolve all claims against Trinity arising from the accident;

- The coverage error in this case was solely the fault of independent agent Rodrian, and was not the fault of any Tower officer or employee;

- Neither Rodrian nor Trinity discovered the coverage error for months, and waited until after the accident occurred before requesting reformation;

- Rodrian carried professional liability insurance with Utica to cover errors exactly like the one he committed in this case;

- Under Wisconsin law, Rodrian's liability carrier could be responsible for covering any claims against the church, because Rodrian had negligently handled the church's insurance application;

- Trinity pursued its Wisconsin-law remedy against Rodrian's liability carrier in this case; and

- There was never any question, either legally or factually, that Trinity would be covered for the accident claims, either by Tower or by Utica.

The only question in this case was whether Trinity's accident-related claims would be paid by Tower or by Utica. Either (in fact, both) were liable for the coverage under Wisconsin law. *Supra* § II.B. Tower thus reasonably believed—consistent with the law—that Utica could be held responsible for the coverage, because its insured (Rodrian) had indisputably committed the error in requesting coverage. Tower, moreover, was entitled under Wisconsin law to assure itself of the facts underlying the coverage dispute before reforming the policy or assuming an obligation that, under Wisconsin law, also could be borne by Utica. Even viewing the evidence in a light most favorable to Trinity, therefore, these undisputed facts belie plaintiff's claim that Tower acted in an intentional disregard of Trinity's rights.

Just as Tower did not intentionally attempt to disregard plaintiff's rights, so Tower's conduct was not "outrageous," or motivated by ill-intent towards plaintiff. Punitive damages therefore are not warranted. *See, e.g., Benke v. Mukwonago-Vernon Mut. Ins. Co.*, 110 Wis. 2d 356, 365, 329 N.W.2d 243, 248 (Wis. Ct. App. 1982) (insureds not entitled to punitive damages when insurer wrongfully failed to pay for insured's loss, as there was no evidence of vindictiveness or malice on part of insurer, even though insurer made up its mind right away that claim was "debatable" and stuck to its belief until it found an expert to back its hypothesis).[7] Indeed, Tower

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[7] *Compare Upthegrove Hardware, Inc. v. Pennsylvania Lumberman's Mutual Ins. Co.*, 146 Wis. 2d 470, 483-84, 431 N. W.2d 689, 695 (Wis. Ct. App. 1988) (affirming punitive damages award where evidence that insurance company (continued...)

is not aware of any Wisconsin case upholding a punitive damages award where the insurer provided a defense for the insured, reformed the insured's policy, and fully paid a claim under that policy. Even viewing the evidence favorably to Trinity, therefore, there is not clear and convincing support for the conclusion that Tower intentionally disregarded Trinity's rights. The Court should vacate the punitive damages award, and either direct a verdict for Tower, or else order a new trial.

3. Tower Is Entitled to a Directed Verdict or a New Trial Because the Court Improperly Admitted Evidence Outside the Scope of the Underlying Bad Faith Ruling

The punitive damages award also cannot stand because it is based on evidence that is beyond the scope of the underlying tort of bad faith. Under Wisconsin law, punitive damages may only be awarded for tortious conduct—such damages are not permitted in contract actions. *See Autumn Grove Joint Venture v. Rachlin*, 138 Wis. 2d 273, 406 N.W.2d 759 (Wis. App. Ct. 1987) (punitive damages are only permitted when there is an underlying tort, not when underlying cause of action is breach of contract); *Weiss*, 197 Wis. 2d 365, 541 N.W.2d 753 (punitive damages are not available as a remedy for breach of contract actions). A finding of bad faith may justify a punitive damage award against the wrongdoer, provided plaintiff also satisfies the higher burden of proving that defendant acted maliciously or with an intentional disregard of plaintiff's rights. *Anderson*, 85 Wis. 2d at 695, 271 N.W.2d at 378; Wis. Stat. § 895.85(3), stats. Punitive damages thus relate to the character of the particular act committed, rather than to plaintiff's theory of

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[7] (...continued)
investigators lied and knowingly destroyed possible critical evidence rose to level of "malice or ill will").

liability. *See Wangen v. Ford Motor Co.*, 97 Wis. 2d 260, 269, 294 N.W.2d 437, 443 (Wis. 1980) (*citing Entzminger v. Ford Motor Co.*, 47 Wis. 2d 751, 757-58, 177 N.W.2d 899, 903 mss. 1970)).

To establish the ill-intent necessary to recover punitive damages, "something must be shown over and above the mere breach of duty for which compensatory damages can be given; that is, a showing of bad intent deserving punishment, or something in the nature of special ill-will towards the person injured . . . ." *Wangen*, 97 Wis. 2d at 268, 294 N.W.2d 437 (quoting *Meshane v. Second St. Co.*, 197 Wis. 382, 387, 222 N.W. 320, 322 (Wis. 1928)).

In the instant case, the Court ruled that "Tower acted in bad faith by not investigating or not properly investigating" plaintiffs' reformation request. (*See* Ruling on Mot. for Summ. J. at 9.) Therefore, the only issue left for trial in this case was whether the allegedly improper investigation of plaintiffs' claims—the sole basis of the Court's bad faith finding—was sufficient to support a punitive damages award, and if so, the magnitude of such award.

Despite this narrow focus, the Court permitted plaintiff to present irrelevant evidence relating to other events not at issue in the bad faith tort, thereby tainting the verdict.[8] Specifically, over Tower's objections, the Court allowed plaintiff to present evidence relating to issues extraneous to the underlying tort of

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[8] Under the principles set forth in *Wangen v. Ford Motor Co.*, 97 Wis. 2d 260, 294 N.W.2d 437 (Wis. 1980), any punitive damages award in this case must relate to conduct motivated by "bad intent" or "special ill-will." *Id.* at 268, 294 N.W.2d at 443. As such, the punitive award must be linked to the conduct this Court deemed to be in bad faith, i.e., the allegedly deficient investigation, which ended by 1996.

bad faith, including, *inter alia*, Tower's motion for summary judgment on the contract reformation claim. By presenting evidence of events that occurred after the Company completed its investigation (i.e., after the Company had allegedly committed the bad faith tort), plaintiff unilaterally enlarged the time and scope of what conduct the jury could punish with a damages award, contrary to basic principles of relevancy, and without any supporting authority. Plaintiff thus blurred the fine between the evidence relating to the underlying tort, and other conduct that had no bearing on that ruling. The latter evidence was not relevant to the issues to be decided by the jury, and was therefore improperly admitted.[9]

"[A]s a matter of law, a judge has no discretion to admit irrelevant evidence." *Bittner v. American Honda Motor Co.*, 194 Wis. 2d 122, 147, 533 N.W.2d 476, 486 (Wis. 1995); Wis. Stat. § 904.02, stats. Further, the evidence was unfairly prejudicial, and prompted the jury to base its punitive damages verdict on matters not properly before it. *See Bittner*, 194 Wis. 2d at 147-48, 533 N.W.2d at 486 (evidence is "unfairly prejudicial" if, *inter alia*, it tends to influence outcome of case by improper means, or causes jury to base its decision on something other than established propositions in the case). This constituted reversible error. Tower is entitled to a directed verdict or a new trial. *See, e.g., Lease America Corp.*, 88 Wis. 2d at 402, 276 N.W.2d at 770 (new trial ordered where evidence was improperly admitted).

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[9] *See* Wis. Stat. § 904.02, stats. (relevant evidence is generally admissible; irrelevant evidence is inadmissible); *see also* Wis. Stat. § 904.01, stats. (relevant evidence has "any tendency to make the existence of any fact that is of consequence to the determination of the action more or less probable than it would without the evidence").

B. Tower Is Entitled to Judgment Notwithstanding the Verdict

1. Standards for Judgment Notwithstanding the Verdict

The Court may grant a motion for judgment notwithstanding the verdict in the event that the "verdict is proper but, for reasons evident in the record which bear upon matters not included in the verdict, the movant should have judgment." Wis. Stat. § 805.14(5)(b), stats. Judgment notwithstanding the verdict does not challenge the sufficiency of the evidence to support the verdict; instead "[a) motion for judgment notwithstanding the verdict admits for purposes of the motion that the findings of the verdict are true, but asserts that judgment should be granted the moving party on grounds other than those decided by the jury." *Management Computer Servs. Inc. v. Hawkins, Ash, Baptie & Co.*, 206 Wis. 2d 158, 175, 557 N.W.2d 67, 74 (Wis. 1996) (quoting *Kolpin v. Pioneer Power & Light Co., Inc.*, 162 Wis. 2d 1, 28, 469 N.W.2d 595, 606 (Wis. 1991) (internal quotations omitted)).[10]

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[10] For example, a trial court should enter judgment notwithstanding the verdict where the facts found by the jury are "insufficient, though admitted, to constitute a cause of action." *Wozniak v. Local # 1111 of the United Elec., Radio & Mach. Workers of America,* 57 Wis. 2d 725, 733, 205 N. W.2d 369, 373 (Wis. 1973) (quoting *State v. Escobedo*, 44 Wis. 2d 85, 90-91, 170 N.W.2d 709, 711 (Wis. 1969) (explaining that "a motion notwithstanding the verdict amounts to a post-verdict motion for a directed verdict")).

2. Because the Court Incorrectly Granted Summary Judgment for Plaintiff, and Erred in Admitting Irrelevant and Inadmissible Evidence at Trial, Tower Is Entitled to Judgment Notwithstanding the Verdict

The punitive damages verdict in this case is based on two faulty premises: (1) an erroneous summary judgment ruling that Tower acted in bad faith (*supra* § III); and (2) evidence of actions by Tower that are beyond the scope of the bad faith ruling (*supra* § IV.A.3). Both of these premises were before the jury at trial: the Court and plaintiff repeatedly advised the jury that Tower had been found to have acted in bad faith, and plaintiff presented (and the Court admitted) substantial evidence regarding alleged conduct by Tower that was beyond the scope of the tort as to which the Court held Tower was liable.

Even assuming *arguendo* that the verdict was "proper" in light of the evidence presented, the fact that Tower was entitled to summary judgment on bad faith, or at least was entitled to have the issue tried to a jury, requires the Court to vacate the punitive damages award and grant judgment for Tower, notwithstanding the verdict. *See* Wis. Stat. § 805.14(5)(b), stats. Stated differently, because plaintiff was not entitled to summary judgment (or any judgment) on bad faith, and because the Court erred in admitting the bad-faith ruling at trial, matters not reflected in the verdict, but contained in the record, require judgment for Tower.

Further, judgment n.o.v. is appropriate because the Court permitted plaintiff to present evidence relating to matters beyond the scope of the underlying tort of bad faith. (*See supra* § IV.A3.) Even assuming *arguendo* the verdict is proper in light of the (improperly admitted) evidence, therefore, matters not reflected in the verdict require judgment for Tower. (*Supra*

§ IV.A.2.) The Court should grant judgment notwithstanding the verdict to Tower.

C. Because the Court Erroneously Admitted the Improper Opinion Testimony of Robert Niendorf, the Punitive Damages Award Is Irretrievably Tainted, and a New Trial Should Be Ordered to Correct the Error

The Court erred in allowing plaintiff to present to the jury the improper opinion testimony of Robert Niendorf. Over Tower's objections and motion to bar his testimony, the Court admitted Niendorf s conclusion that Tower is able to pay a punitive damages award in one of three ways: by liquidating its assets (at the end of 1999, the Company had a net worth of $24.6 million); by drawing on insurance reserves, or "retained earnings," for a sum of approximately $15 million; or by restructuring its debt-equity ratio, allegedly yielding $18.7 million. As Tower has explained, Niendorf s analysis improperly aggregates the financial position of Tower and its parent company, Atlas Assurance Company of America ("Atlas"). Niendorf's conclusions, moreover, are premised on the notion—contrary to Wisconsin law—that the jury can reach non-party Atlas's assets in order to finance an award against Tower. Although the Court redacted the portions of Niendorf's testimony in which he described his premise (that he had included Atlas's finances in assessing what amount Tower could afford to pay in punitive damages), the Court permitted Niendorf to testify to his conclusions. This ruling did not cure the problem.[11] Simply not telling the jury about a premise that

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[11] If anything, the Court's ruling exacerbated the problems in Niendorf's testimony. By slicing out all references to Atlas in Niendorf's testimony, the Court took away the jury's ability to decide whether Tower's assets should be co-mingled with its parent's, and thereby artificially inflated Tower's assets.

is contrary to law, while permitting testimony that is expressly based on that unlawful premise, does not remove the error.

Under Wisconsin law, punitive damages cannot be based on the assets of a non-party parent corporation. Rather, only evidence of a *defendant's* wealth and ability to pay is relevant to the issue of punitive damages. *Fahrenberg v. Tengel*, 96 Wis. 2d 211, 225, 291 N.W.2d 516, 522 (Wis. 1980) (evidence of defendant's wealth was relevant in assessing the amount to be awarded as punitive damages despite fact that plaintiff did not seek punitive damages from two other co-defendants). As the Wisconsin Supreme Court has explained, punitive damages are designed as "individualized punishment of a wrongdoer whose conduct toward the plaintiff is particularly outrageous. Implicit in this concept is the notion that, where punishment is to be exacted, it must be certain that the wrongdoer being punished because of his conduct actually caused the plaintiffs injuries." *Collins v. Eli Lilly Co.*, 116 Wis. 2d 166, 202, 342 N.W.2d 37, 54 (Wis. 1984) (plaintiff who sued multiple defendants, but could not prove which defendant caused her injuries, could not recover punitive damages). Because punitive damages are "intended as a personal penalty for the actual wrongdoer, [the extension of punitive damages] to others who were not themselves the actual perpetrators of the conduct should be limited." *Franz v. Brennan*, 150 Wis. 2d 1, 8-9, 440 NW.2d 562, 566 (Wis. 1989) (holding that evidence of defendant's parents' wealth was irrelevant to assessment of punitive damages against minor involved in car accident, and that punitive damages could not be assessed against defendant's parents).

As a matter of law, a jury may not punish Tower by taking money from Tower's nonparty parent. *See, e.g., HCA Health Servs. v. National Bank of Commerce*, 745 S.W.2d 120, 124 (Ark. 1988) (error to permit plaintiff to refer to parent health care company in quest for punitive damages); *Liberty Fin. Mgmt. Corp. v. Beneficial Data Processing Corp.*, 670 S.W.2d 40, 51-52 (Mo. Ct. App. 1984) (error to allow financial infor-

mation about parent consumer finance company in suit against subsidiary); *Walker v. Dominick's Finer Foods, Inc.*, 415 N.E.2d 1213, 1217 (Ill. App. Ct. 1980) (error to admit net sales of defendant's non-party parent corporation, despite fact that defendant was wholly-owned subsidiary of parent). Niendorf's analysis, however, instructed the jury to do just that. By including the net worth of Tower's parent in the calculation of punitive damages, Niendorf's testimony ran counter to Wisconsin law, urged the jury to take unlawful action, and necessarily tainted the verdict.[12]

By failing to exclude evidence that does not meet the standards of Wisconsin law, the Court unfairly prejudiced the outcome in this case. *See, e.g., Lease America Corp.*, 88 Wis. 2d at 401, 276 N.W.2d at 770 ("Evidence is unfairly prejudicial if it has 'a tendency to influence the outcome by improper means' or if it 'appeals to the jury's sympathies, arouses its sense of horror, provokes its instinct to punish' or otherwise causes a jury to 'base its decision on something other than the established propositions in the case'") (citations omitted). Niendorf's testimony conflated the assets of the defendant and a separate non-party corporation, inaccurately inflated the sum of money Tower allegedly has available to finance a punitive damages award, and invented a safety net for Tower (in the form of financial backing by Atlas). As such, the punitive damage verdict in this case is irretrievably infected by error and must be vacated. The Court should order a new trial on punitive damages.

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12 Plaintiff can avoid this black-letter rule only by presenting evidence that compels the Court to pierce the defendant's corporate veil. Trinity produced absolutely no evidence supporting veil-piercing in the case of Tower.

D. Because the $3.5 Million Punitive Damages Award Against Tower Violates Due Process and the Policies of Wisconsin, the Court Should Vacate the Award, Direct a Verdict for Tower, Order a New Trial, or Issue a Substantial Remittitur

Even assuming away all of the foregoing problems, the $3.5 million punitive damages award in this case—the largest punitive award in the history of Waukesha County—is unconstitutional under the United States and Wisconsin constitutions, and is contrary to Wisconsin law. "The Due Process Clause of the Fourteenth Amendment prohibits a State from imposing a 'grossly excessive' punishment on a tortfeasor." *BMW of N. Am., Inc. v. Gore*, 517 U.S. 559, 562 (1996) (quoting *TXO Prod. Corp. v. Alliance Res. Corp.*, 509 U.S. 443, 454 (1993)).[13] Even prior to *BMW*, the Wisconsin Supreme Court warned that "[a]n award which is more than necessary to serve its purposes . . . or which . . . is disproportionate to the wrongdoing is excessive and is contrary to public policy." *Wangen*, 97 Wis. 2d at 303, 294 N.W.2d at 459. The $3,500,000 award in this case is grossly excessive, and, if not vacated, must be greatly reduced in order to satisfy constitutional and public policy concerns.

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[13] The Fourteenth Amendment provides that no state may "deprive any person of life, liberty, or property, without due process of law." U.S. Const., Amend. XIV, § 1. *See also* Wis. Const. § 1 (outlining "inherent rights"); *Dowhower v. West Bend Mutual Ins. Co.*, 236 Wis. 2d 113, 119, 613 N. W.2d 557, 560 (Wis. 2000) (§ 1 of Wisconsin Constitution sets forth substantive due process provision; there is "no substantial difference" between substantive due process provisions of § 1 and Fourteenth Amendment due process clause).

1. The $3,500,000 Punitive Damage Award Violates Due Process

"Elementary notions of fairness enshrined in our constitutional jurisprudence dictate that a person receive *fair notice* not only of the conduct that will subject him to punishment, *but also of the severity of the penalty that a State may impose*." *BMW*, 517 U.S. at 574 (emphasis added). The Supreme Court identified three guidelines that should direct the analysis of whether a defendant received "adequate notice of the magnitude of the sanction": (1) the degree of reprehensibility of defendant's conduct; (2) the ratio of the punitive damage award to the actual and potential harm inflicted on plaintiff; and (3) comparison of the punitive damage award with the civil or criminal penalties that could be imposed for similar conduct. 517 U.S. at 574; *Jacque*, 209 Wis. 2d at 627, 563 N.W.2d at 164. Under each of these guidelines, the $3.5 million punitive damage award is excessive and unconstitutional.

(a) Reprehensibility

"Perhaps the most important indicium of the reasonableness of a punitive damages award is the degree of reprehensibility of the defendant's conduct." *BMW*, 517 U.S. at 575. The *BMW* Court identified the following factors to be indicative of particularly reprehensible conduct: the presence of violence or physical harm, intentional malice or recidivism, "deliberate false statements, acts of affirmative misconduct, [and] concealment of evidence of improper motive." *Id.* at 576-77, 579; *see also Lee v. Edwards*, 101 F.3d 805, 809-10 (2d Cir. 1996) (identifying presence of violence, deceit or malice and repetition of conduct as aggravating factors in determining degree of reprehensibility).

This case involves no evidence of any such factors. The only injury even arguably inflicted on plaintiff in this case (a $17,000 bill for lawyers Trinity hired to pursue the reformation

claim against Tower) is purely economic in nature, and therefore is "less worthy of large punitive damages awards than torts inflicting injuries to health and safety." *Continental Trend Res., Inc. v. OXY USA Inc.*, 101 F.3d 634, 638 (10th Cir. 1996) (reducing punitive damage award of $30 million to $6 million because harm inflicted by defendant was purely economic and ratio between punitive and compensatory damages was too high).

Additionally, there is absolutely no evidence of malicious intent, affirmative misconduct, or improper motive by Tower. This case involves a dispute between two insurance companies both potentially liable under Wisconsin law—regarding which one would cover Trinity's accident. Under the law, therefore, Tower reasonably (indeed, correctly) believed that Rodrian's errors and omissions insurance carrier could be responsible for covering the claims against Trinity. When Trinity was sued over the accident, and Tower uncovered information in discovery indicating that the policy should be reformed, Tower did so immediately. Meanwhile, Tower had already hired and paid for lawyers to defend Trinity, who effectively defended the insured in the accident litigation. Tower then paid all of the money to resolve all of the claims against Trinity under the reformed policy. Throughout the entirety of these proceedings, Trinity has never been without coverage. Tower's conduct in this case simply does not justify the imposition of such a high punitive damages award.

(b) Proportionality

In addition to the foregoing problem, "exemplary damages must bear a 'reasonable relationship' to compensatory damages." *BMW*, 517 U.S. at 580. The appropriate inquiry is "whether there is a reasonable relationship between the punitive damages award and the harm likely to result from the defendant's conduct as well as the harm that has actually occurred." *Id.* at 581 (emphasis omitted).

The only harm that "actually occurred" or was "likely to result" from Tower's actions was that Trinity was required to pay approximately $17,000 in attorneys' fees to lawyers it hired to pursue a reformation claim against Tower and defend against Tower's summary judgment motion.[14] Accordingly, even where insurance companies have been held liable for bad faith conduct, courts have reduced punitive damages verdicts when jury awards are found to be excessive in comparison to the harm suffered. *See, e.g,, Dixie Ins. Co. v. Mooneyhan*, 684 So. 2d 574, 586 (Miss. 1996) (court found $1 million punitive award for insurance company's bad faith refusal to pay $542 in property damage to be excessive, and remanded for new trial). *See also infra* § IV.E. (discussing remittitur).

Given the remediation of plaintiff's injuries, there is no threat of additional harm. Moreover, "[w]hen the injury is economic and particularly when it arises out of a contractual relationship where the parties can and should contractually protect themselves by providing explicit remedies in the event of breach, the permissible ratio of punitive damages to compen-

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[14] Plaintiffs argument at trial that, in fact, an exposure of $490,000 was "likely to result" from Tower's actions ignores Wisconsin law and the undisputed evidence in the record. Under Wisconsin law, Trinity had (and pursued) causes of action against Tower and against Utica, Rodrian's professional liability carrier. Thus, even assuming arguendo that Tower did not reform the policy and declined to cover the accident, Trinity still had a viable claim against Utica, and would not have gone uncovered. Of course, Tower did reform the policy, did defend the accident case, and did pay to resolve all claims against Trinity. The upshot of this undisputed evidence, and the clear operation of Wisconsin law, however, is that *Trinity was never at risk of not being covered for the accident*. Rather than facing an issue of whether the loss would be covered, the only question was who would cover the loss.

satory damages should be relatively modest." *FDIC v. Hamilton*, 122 F.3d 854, 862 (10th Cir. 1997).

The 200:1 ratio of punitive to compensatory damages ($3,500,000:$17,000) in this case is unjustified and unconstitutional. Although the *BMW* Court eschewed any precise mathematical formula for punitive damages, it appeared to regard punitive damages awards of more than ten times the amount of either the actual or potential harm to plaintiff to be dangerously close to the boundary of constitutional infirmity. *BMW*, 517 U.S. at 581. Moreover, the ratio between punitive and compensatory damages here far exceeds the ratio of punitive damages awards imposed on other insurance companies in other bad faith actions. *See, e.g., Ace v. Aetna Life Ins. Co.*, 139 F.3d 1241, 1248 (9th Cir. 1998) (finding punitive damage award of $16.5 million, reflecting a 130:1 ratio of punitive-to-compensatory damages, to be excessive); *Egan v. Mutual of Omaha Ins. Co.*, 620 P.2d 141, 149 (Cal. 1979) (award of $5 million in punitive damages against insurer for breach of implied covenant of good faith and fair dealing was excessive as a matter of law because it represented 40 times the compensatory damages assessed); *Paramount Nat'l Life Ins. Co. v. Williams*, 772 S.W.2d 255, 268 (Tex. App. 1989) (finding 10:1 ratio of punitive to compensatory damages for insurer's breach of its duty of good faith and fair dealing to be excessive).[15] In short, no precedent supports

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15 Nor does the ratio of punitive-to-compensatory damages here fare better when compared to punitive damages awards considered to be constitutional in other areas of the law. *See, e.g., Management Computer Servs. v. Hawkins, Ash. Baptie Co.*, 206 Wis. 2d 158, 196, 557 N.W.2d 67, 83 (Wis. 1996) (finding ratio 27:1 to be excessive, but approving award of punitive damages equal to compensatory damages); *TXO Prod. Core. v. Alliance Res. Corp*, 509 U.S. 443, 459-460 (1993) (finding ratio of 10:1 to be constitutional); *Gianoli v. Pfleiderer*, 209 Wis. 2d 509, 563 N.W.2d 562 (Wis. Ct. App.

(continued...)

the 200:1 ratio of punitive damages to compensatory damages in this case, given the harms and conduct at issue.

(c) Comparability

The final guideline for determining whether a tortfeasor had sufficient notice of the severity of the penalty is a comparison to civil and criminal penalties that could have been imposed for comparable misconduct. *BMW*, 517 U. S. at 583. The purpose of referring to comparable penalties is to determine whether the defendant had fair notice of the punitive penalty at the time the act occurred. *BMW*, 517 U.S. at 574.

Wisconsin insurance law provides that the Insurance Commissioner can assess a criminal penalty of "not more than $10,000" against a corporation that intentionally violates any state insurance statute or rule, including the duty to settle claims in good faith. *See* Wis. Stat. § 601.64(4).[16] The $3.5 million

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15 (...continued)
1997) (ratio of 15:1 is not grossly excessive); *Dalton v. Meister*, 52 Wis. 2d 173, 188 N. W.2d 494 (Wis. 1971) (punitive damages equal to compensatory damages are reasonable); *Romano v. U-Haul Int'l*, 233 F. 3d 655, No. 99-2328, 2000 WL 1774117 (1st Cir. 2000) (approving ratio of 19:1); *cf. BMW of N. Am. v. Gore*, 517 U.S. 559, 583 (1996) (finding ratio of 500:1 to be excessive, and enough to "raise a suspicious judicial eyebrow").

16 Under the Wisconsin Administrative Code, the Insurance Commissioner may commence an action against an insurance company and subject it to penalties pursuant to Section 601.64 of the Wisconsin Statutes for unfair settlement practices. *See* Wis. Admin Code Ins. 6.11(3)(x)(4); Wis. Stat. § 601.64(4). Unfair settlement practices include the "failure to attempt in good faith to effectuate fair and equitable settlement of claims submitted in which liability
(continued...)

penalty in this case is *350 times* the amount the Insurance Commissioner is legally allowed to sanction for misconduct under Wisconsin law. Tower had insufficient notice that its actions could potentially result in such a staggering penalty. Given that the punitive damages award in this case is grossly disproportionate to the statutory penalties governing similar conduct, the verdict cannot stand.

2. The $3,500,000 Punitive Damage Award Violates the Policies of Wisconsin

"The purpose of punitive damages is to punish the wrongdoer and to deter the wrongdoer and others from similar conduct." *Management Computer Servs.*, 206 Wis. 2d at 193, 557 N.W.2d at 83; *see also Lisowski v. Chenenoff*, 37 Wis. 2d 610, 633, 155 N.W.2d 619, 631 (Wis. 1968) ("punitive damages are assessed not to compensate the injured party but as a punishment to the tortfeasor and as a deterrent to others"). "An award which is moi a than necessary to serve its purposes . . . is contrary to public policy." *Wangen*, 97 Wis. 2d at 303, 294 N. W.2d at 459. As the Supreme Court of Wisconsin has instructed, "in determining whether an award of punitive damages is excessive, courts should consider the grievousness of the acts, the degree of malicious intent, whether the award bears a reasonable relationship to the award of compensatory damages, the potential damage that might have been caused by the acts, the ratio of the award to civil or criminal penalties that could be imposed for comparable misconduct, and the wealth of the wrongdoer." *Management Computer Servs.*, 206 Wis. 2d at 194, 557 N.W.2d at 82. The punitive damages award in this case far

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16 (...continued)
has become reasonably clear." Wis. Admin. Code. Ins. 6.11(3)(x)(4).

exceeds any amount appropriate to serve this state's interests in punishment and deterrence.

(a) Punishment

The appropriate retribution for a defendant's misconduct turns on the degree of reprehensibility. As described in detail *supra* § III.C.1.a., the conduct in this case in no way supports a punishment so extreme. The record here is devoid of any indication of malicious intention or evil conduct by Tower, and does not support a finding of intentional disregard.

(b) Deterrence

The punitive damages award in this case also does not create a meaningful deterrent with respect to future conduct. As to specific deterrence of Tower, the record establishes that Tower is no longer in the insurance business. The Company no longer sells or underwrites insurance, and at this point has no employees. Consequently, Tower does not pose any threat of future misconduct, and "deterring" Tower at this point is an empty proposition.

Further, to the extent general deterrence is warranted on the facts of this case, less drastic remedies would achieve the goal. As the United States Supreme Court has held, "[t]he sanction imposed . . . cannot be justified on the ground that it was necessary to deter future misconduct without considering whether less drastic remedies could be expected to achieve that goal." *BMW*, 517 U. S. at 584. Certainly, a less extreme remedy than a punitive damages award against a now-defunct company that is two hundred times the amount of compensatory damages would serve as an effective deterrent of other companies in the future. In short, a punitive damages award of $3.5 million in this case is "shocking to the conscience," and should be vacated. *See Management Computer Servs.*, 206 Wis. 2d at 196, 557 N.W.2d at 83 (mandating remittitur of punitive

damage award of $1.75 million, despite fact that defendant's conduct was reprehensible and required substantial penalty to punish and deter, because award was more than necessary to serve purposes of punitive damages, and was considerably greater than compensatory damages of $65,000).

E. In the Event the Punitive Damages Award is Not Vacated, the Court Should Issue a Remittitur to Comport with Due Process

Absent an order vacating the punitive damages award altogether, the Court should significantly reduce the verdict in this case. The Court has the authority to issue a remittitur, and "to reduce the amount of punitive damages to what it determines is a fair and reasonable amount for such kind of damages." *Malco, Inc. v. Midwest Aluminum Sales, Inc.*, 14 Wis. 2d 57, 65, 109 N.W.2d 516, 521 (Wis. 1961). The Court should exercise that authority to reduce excessive damages awards to a reasonable level. *Unified Catholic Schools of Beaver Dam Educational Ass'n v. Universal Card Servs. Corp.*, 34 F. Supp. 2d 714, 718 (E.D. Wis. 1999) (under Wisconsin law, jury award of punitive damages is subject to control of trial court, which has power to reduce punitive damages to amount it deems fair and reasonable in fight of defendant's conduct). *See also Honda Motor Co. v. Oberg*, 512 U.S. 415, 432 (1994) (because "[p]unitive damages pose an acute danger of arbitrary deprivation of property," courts are vested both by statute and by Constitution with independent obligation to ensure that punitive damages are not excessive, and to enter a remittitur to rectify injustices); *Management Computer Servs.*, 206 Wis. 2d at 193-195, 557 N.W.2d at 81-83 (court should determine whether the punitive damages award is excessive and decide the proper amount to be awarded as punitive damages); *Wangen*, 97 Wis. 2d at 298, 294 N.W.2d at 457 (emphasizing importance of "[j]udicial controls. . . in this state . . . for determining the amount of the punitive damages award which will serve the punishment and deterrent objectives of punitive damages,

without inflicting a penalty on a defendant disproportionate to the defendant's wrong and contrary to the public interest.").[17]

Without a substantial remittitur, the record $3.5 million punitive damages verdict in this case violates basic principles of due process. In determining the appropriate amount of punitive damages, the Court must consider the following factors: the grievousness of the wrongdoer's acts, the degree of malicious intent, the potential and actual damage that must have been caused by such acts, and the defendant's ability to pay. *See Gianoli v. Pfleiderer*, 209 Wis. 2d 509, 528, 563 N.W.2d 562, 569 (Wis. Ct. App. 1997). *See also Management Computer Servs.*, 206 Wis. 2d at 194, 557 N.W.2d at 82 (enumerating factors court should consider in determining whether award is excessive)).

The circumstances of this case highlight the need for remittitur. *See id.* at 194, 557 N.W.2d at 82 ("[A] reviewing court must consider the reasonableness of punitive damages on a case-by-case basis, considering the relevant circumstances in each particular case."). First, there is no evidence and no allegation that Tower acted maliciously. Second, both as a matter of law and as a matter of fact, Trinity has never been at risk of not being covered by insurance for the accident. The only issue was which insurance company would cover the claim. Third, there is no question that the jury's analysis of punitive damages was tainted by the improper testimony of the only damages witness in the case (Niendorf), whose calculations were based on the wealth of Tower's parent, and not Tower itself. Fourth, the punitive damages awarded here are grossly disproportionate to compensatory damages - a 200-to-1 ratio. Fifth, the Court's novel and premature summary judgment

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17 Wis. Stat. § 805.15(6), stats., also authorizes the Court to reduce the punitive award in this case, as part of the Court's power to order a new trial

ruling, combined with the admission of improper evidence at trial, renders the proceedings in this case highly irregular, undermining confidence in any verdict.

Under these circumstances, the record $3.5 million punitive damages award in this case cannot stand. This Court should follow the numerous courts that have reduced other excessive bad faith punitive damages awards against other insurers. *See, e.g., Buzzard v. Farmers Ins. Co.*, 824 P.2d 1105, 1115 (Okla. 1992) (court reduced $2 million bad faith punitive damages award to $400,000 because evidence improperly influenced jury and created an improper sympathetic response); *Mutual Life Ins. Co. v. Estate of Wesson*, 517 So. 2d 521, 533 (Miss. 1987) (court reduced $8 million bad faith punitive damages award by $6.5 million, to $1.5 million, holding award was excessive where no human life or injury was threatened); *Aetna Life Ins. Co. v. Lavoie*, 505 So. 2d 1050, 1053-54 (Ala. 1987) (court reduced $3.5 million bad faith punitive damages award by $3 million, to $500,000, holding that verdict was excessive in light of gravity of the wrong and injury inflicted upon insured); *Safeco Ins. Co. v. Ellinghouse*, 725 P.2d 217, 227 (Mont. 1986) (court reduced $5 million bad faith punitive damages award to $1 million, because award was "so grossly excessive and disproportionate to the injury as to shock one's conscience"); *Timmons v. Royal Globe Ins. Co.*, 653 P.2d 907, 918-19 (Okla. 1982) (court reduced $3 million bad faith punitive damages award to $1. 5 million where award resulted from jury's improper sympathies); *State Farm Mut. Auto. Ins. Co. v. Zubiate*, 808 S.W.2d 590, 605-06 (Tex. App. 1991) (court reduced $15 million bad faith punitive damages award by over $14.3 million, to $660,000, because injuries suffered by insured were not life threatening).

The $3.5 million punitive damages award in this case constitutes a windfall bearing no relationship to the underlying purposes of a punitive award. The award should be vacated or substantially reduced. *See Lenard v. Argento*, 699 F.2d 874, 890

(7th Cir. 1983) (punitive damages should not go beyond deterrence and become a windfall). Given that the punitive damages assessed in this case greatly exceed the amount necessary to effectuate the purposes of punishment and deterrence, and inflict a penalty on Tower that is wholly disproportionate to the acts in question (*supra* §§ III.C., D.), the Court should fulfill its obligation under the law by vacating or reducing the excessive punitive damages award in this case.

V. CONCLUSION

For the foregoing reasons, Tower respectfully requests that the Court reverse its *sua sponte* order granting summary judgment for plaintiff in this case, and grant summary judgment based on the undisputed facts in favor of Tower. Alternatively, the Court should conduct a trial to resolve any genuine issues of fact as to whether Tower acted in bad faith. Tower further requests that the Court vacate the punitive damages award in this case, and grant its motions for directed verdict, judgment notwithstanding the verdict, new trial, or remittitur.

Dated at Milwaukee, Wisconsin, this 10th day of January, 2001.

BORGELT, POWELL, PETERSON & FRAUEN, S.C.
Attorneys for Defendant
Tower Insurance Company
By:/s/ Patrick S. Nolan
M. M. Christine Cowles (SBN 1005158)
Barbara A. O'Brien (SBN 1018341)
Patrick S. Nolan (SBN 1024491)
735 Water Street, Suite 1500
Milwaukee, Wisconsin 53202-4188

OF COUNSEL

Edward M. Crane
Charles F. Smith
Eric J. Gorman
Victoria A Birov
SKADDEN, ARPS, SLATE,
MEAGHER & FLOM (Illinois)
333 West Wacker Drive, Suite 2100
Chicago, Illinois 60606